Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
Review of Regulatory Requirements for Incumbent LEC Broadband Telecommunications Services	)	**CC Docket No. 01-337**

COMMENTS OF AT&T CORP.

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March 1, 2002

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AT&T Corp. ("AT&T") respectfully submits these comments in response to the Commission's Notice of Proposed Rulemaking.[1]

INTRODUCTION AND SUMMARY

The *Notice* seeks comment on whether certain of the "broadband" services of dominant incumbent local exchange carriers ("ILECs") should be exempted from the tariffing, cost support, and related rate regulations that apply to other ILEC services. The *Notice* states that, although these dominant carrier regulations will continue to apply to all of the ILECs' "narrowband" services and to the broadband services they offer under their special access tariffs, the largest ILECs now contend that they lack market power in the provision of other broadband services. More specifically, the *Notice* seeks comment on SBC's extraordinary request for a

[1] *Review of Regulatory Requirements for Incumbent LEC Broadband Telecommunications Servs.*, FCC 01-360, 2001 WL 1636518 (Dec. 20, 2001) ("*Notice*").

blanket and immediate declaration of non-dominance with respect to all of its "broadband" services – which SBC defines as *any* service with 56 kbps or greater bandwidth.[2]

The SBC Petition, as baseless and overbroad as it is, is just the tip of the media-generated iceberg to which the ILECs have relentlessly attempted to steer public policy in the past two years. In an extraordinary and unprecedented campaign aimed at the Commission, Congress, and anyone else that will listen, the ILECs have conjured a broadband "crisis" to support myriad proposals that, taken together, would dismantle virtually the entire regulatory framework designed to reward consumers by supplanting the ILECs' enduring bottleneck monopolies with competition.

The ILECs have petitioned to deny unbundled access to high-capacity loops and dedicated transport.[3] They have argued for restrictions on competitors' use of combinations of loop and transport network elements.[4] They have sought to withhold access to "next generation" loops.[5] And to round out their monopolization wish list, the ILECs have asked the Commission to relieve them of all line sharing and line splitting obligations,[6] to forbid competitive local

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[2] *See* SBC Petition for Expedited Ruling That It Is Non-Dominant in Its Provision of Advanced Services and for Forbearance from Dominant Carrier Regulation of Those Services, at 2, 30 ("SBC Petition").

[3] *See* Joint Petition of BellSouth, SBC, and Verizon, *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996; Elimination of Mandatory Unbundling of High-Capacity Loops and Dedicated Transport*, CC Docket No. 96-98 (Apr. 5, 2001).

[4] *See generally*, Supplemental Order Clarification, *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, 15 FCC Rcd. 9587, CC Docket No. 96-98 (2000) ("*Supplemental Order Clarification*").

[5] *See e.g.*, Comments of SBC, *In the Matter of Deployment of Wireline Services Offering Advanced Telecommunications Capability*, CC Docket No. 98-147, at 65-71 (Oct. 12, 2000).

[6] *See* Comments of Verizon, *Inquiry Concerning High-Speed Access to the Internet Over Cable and Other Facilities*, GN Docket No. 00-185, at 27-28 (Dec. 1, 2000); Comments of (continued …)

exchange carriers ("CLECs") that pay for entire "loops" from offering any data services over those loops,[7] to terminate all broadband-related collocation obligations, to lift the § 254(c)(4) resale requirement, and to forbear from applying the requirements of § 271 to any advanced services.[8]

All of the ILEC proposals that make up this anticompetitive campaign must be considered in the context of the glaring falsehoods and economic doublespeak upon which they are built. The ILECs claim, for example, that regulation is preventing them from investing in broadband upgrades, causing their digital subscriber line ("DSL") services to wither on the vine, and tilting the playing field in favor of the cable firms against whom they compete for certain customers. Reality bears no resemblance to this fictional tale. The reality is that ILECs are continuing to upgrade their facilities and to add new electronics, and they have no plans to stop. Their business decisions to spend billions of dollars on these upgrades have nothing to do with the tariffing and other pro-competitive regulations they challenge – which impose costs that, by comparison, are truly *de minimis* – and everything to do with the enhanced profits they expect to earn if they invest and the profits they expect to lose if they cede the field to others.

DSL is thriving and growing much faster than cable modem service, as the ILECs' own public statements confirm. Indeed, the ILECs' DSL services, once removed from the shelves upon which they collected dust for many years, have experienced acceptance and

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(… continued)

SBC/BellSouth, *Inquiry Concerning High-Speed Access to the Internet Over Cable and Other Facilities*, GN Docket No. 00-185, at 19-23 (Dec. 1, 2000).

[7] *See id*. at 20 n.55.

[8] *See id*. at 19-23.

growth rates that rival the most successful consumer products of all time. Any recent slowing in ILEC growth rates is a product not of regulation, but of the incumbents' well-publicized price hikes and customer service failures. And the reality is that there is no broadband crisis at all. Broadband is already available to more than 80% of Americans; most people simply have chosen not to buy it.

It is quite absurd that the ILECs would claim that they need relief from the Commission to protect them from their rivals. ILECs have monopolies over the bottleneck inputs necessary to provide broadband services to virtually all business customers (large and small), as well as to the residential customers located in the many areas where there is no cable modem service. There is no intermodal competition for these services, and the ILECs have used their control over bottleneck facilities to prevent the development of any effective "intramodal" competition. Through their relentless campaigns of litigation, discrimination, and outright refusal to obey the requirements of the Telecommunications Act of 1996, the ILECs have already put most of their CLEC and data-LEC ("DLEC") competitors out of business, and those that remain have sharply scaled back their operations. Rather than grant further regulatory relief to the ILECs, the Commission's primary tasks should be to enforce the requirements of §§ 251(c) and 252(d) that ILECs provide nondiscriminatory access to their bottleneck facilities and to close the loopholes that have enhanced the ability of the ILECs' to evade these duties.

The ILECs do compete with cable operators in providing broadband services to residential customers in many places. But the ILECs are, to say the least, holding their own against their cable rivals. The most recent reports, for example, indicate that the ILECs had their largest DSL gains ever in the fourth quarter of 2001 – even in the face of their decision to initiate an extraordinary 25% in their broadband prices. And the fact that ILECs found it profitable to

increase prices so sharply – at the same time that DSL providers in other countries are *cutting* their prices – by itself refutes the ILECs' claims that the Commission can simply assume that they lack market power wherever cable competition exists.

To be sure, the issues raised in the *Notice* are, on their face, narrow and do not implicate the full range of arguments that the ILECs have advanced in their assault on the 1996 Act. This proceeding purports to consider only the "tariffing," cost support, and related regulations that can help detect price squeezes and otherwise enforce the requirements of §§ 201-202 that ILECs' services be offered at rates, terms, and conditions that are just, reasonable, and nondiscriminatory. As explained below, these dominant carrier regulations will continue to play a vital role so long as the ILECs retain market power. By contrast, the costs that these regulations impose on the ILECs are truly *de minimis*. SBC does not even attempt to quantify them, much less to contend that they are actually interfering with its ability to invest in broadband or to compete effectively in providing broadband services.

The proper treatment of the SBC Petition and the more general questions raised in the *Notice* should be clear. Under the Commission's precedents, an ILEC request for an exemption from dominant carrier regulation for a particular service offering cannot be granted unless the ILEC can demonstrate that it lacks any relevant market power with respect to that service. That is a showing that has not been made by SBC and could not be made by any ILEC with respect to most or all broadband services – even if broadband and narrowband services are deemed to be separate markets despite the overwhelming evidence that they are reasonably substitutable services for the vast majority of consumers.

The ILECs unquestionably have market power over the bottleneck inputs necessary to provide broadband services to large and small business customers. There is no

material (or prospective) intermodal competition from cable operators or others. Moreover, the ILECs have used their control over their bottleneck exchange facilities to prevent the development of effective intramodal competition and to monopolize the provision of retail services to the business customers they have not been prohibited (by the interLATA restriction) from serving.

The ILECs also have pervasive market power over broadband services used by residential customers. That is starkly the case in the areas in which ILECs provide DSL but in which cable operators are not providing cable modem services. As the Commission has recognized, the level of competitive broadband activity varies considerably from one locale to the next, and the Commission's precedents therefore plainly bar the blanket market power determinations that SBC seeks. If any ILEC request for an exemption from dominant carrier regulation is to be granted, it must be on the basis of a showing that the ILEC lacks market power with respect to a particular service provided to a particular class of customers in particular geographic areas.

That requires far more than simply showing that cable modem service is available in the locale in question, for the ILECs have not shown that they lack market power even in those areas in which they do face competition from cable operators. Market power is the power profitably to raise (and maintain) prices, and the ILECs' 25% price increases confirm that they, at least, believe they can do that. The ILECs could raise prices even in the face of cable competition, because: (1) many customers value the ability to obtain broadband service from the same firm that provides narrowband voice service (generally only the ILEC) and would pay the higher price; and (2) although other customers discontinued ILEC DSL service in response to the price hike (or refused to buy ILEC DSL service that they would have purchased at the lower

price), many of these customers substituted second telephone lines or other ILEC services that are more profitable to the ILECs. In short, the ILECs' narrowband monopolies – and their control over the facilities used to provide *both* broadband and narrowband services – give them market power over residential broadband services even where there is competition from cable.

Of course, even if it could be shown that ILECs do not have market power in the provision of some broadband services to some customers in some areas, it would be entirely artificial, arbitrary, and impractical for the Commission to try to maintain and enforce one set of dominant carrier rules for these broadband services and a different set for the ILECs' other services. The arbitrariness – and danger – of ignoring the clear interrelationships between narrowband and broadband is highlighted by the *Notice's* failure to provide any definition that would distinguish one from the other. Both services offer the same basic functionality (a means of connecting to the Internet), both offer voice capability as well, both are offered over the same ILEC copper wires, and, until the ILECs' recent DSL price hikes, both cost the consumer roughly the same price. No party has identified any economic support for the conclusion that 200 kbps (the numeric distinction that the Commission has employed in past) is the point at which "narrowband" services (provided at lower speeds) are no longer readily substitutable for "broadband" services; there certainly is none for SBC's preposterous 56 kbps proposal.

Because arbitrary distinctions between "narrowband" and "broadband" are divorced from economic reality, the danger is high that deregulating "broadband" would create loopholes that would allow ILECs to evade regulation of their traditional services. A distinction based on an arbitrary speed boundary is especially troubling. With Regional Bell Operating Companies ("RBOCs") and other ILECs aggressively pushing fiber closer and closer to the home, it is likely that most or *all* ILEC access lines will soon support speeds of greater than

56kpbs, and that distinctions between the low frequency and high frequency portion of loops will become increasingly meaningless. At the same time, voice services increasingly will be IP-based. But none of this will change the unfortunate reality that ILECs will continue to control virtually all of the last-mile facilities over which voice services are delivered. Although cable telephony is promising, it will still be many years (if at all) before that service is widely available throughout the country. In this environment, exempting ILEC "broadband" services from regulation creates a very real risk that ILECs will evade much-needed regulation of services and facilities over which their dominance cannot be questioned.

The price of letting that happen could be very high indeed, for the result may be to crush already fragile attempts at competitive entry into local telephone markets. By contrast, the price of an (unlikely) error in the other direction – maintaining existing regulations that the ILECs claim are unnecessary – is quite low, for the ILECs cannot show that the tariffing and related dominant carrier regulations impose any significant costs or impediments to competition with cable. In these circumstances, no shortcuts or superficial analysis can be tolerated; no broadband services should be exempted from dominant carrier regulation absent clear, comprehensive, and convincing proof that there is no risk of abuse of market power, and that evidence certainly cannot be found in the SBC Petition.

These comments are divided into four parts. Part I addresses the legal standard governing the Commission's determination of non-dominance and demonstrates that, contrary to SBC's contention, the Commission cannot make a blanket determination that all ILEC broadband services are non-dominant based solely on the ILECs' low national average shares. Rather, the Commission must assess the significance of the ILECs' local bottlenecks in rigorously defined local and point-to-point markets. It must then refuse to classify broadband

services as non-dominant if there are markets in which ILECs have market power or in which reclassification of these services would impair the regulation of the ILECs' remaining concededly dominant services. Part II applies this standard to the relevant local markets and summarizes the considerable evidence of pervasive ILEC market power.

Part III demonstrates that, because the ILECs have pervasive market power over the provision of broadband services, the Commission's dominant carrier tariffing, cost support, and related requirements must continue to apply and, in fact, are necessary to ensure effective enforcement of wholesale access requirements and detection of anticompetitive price squeezes and other unjust, unreasonable, and discriminatory practices. But the same market power considerations also confirm that the Commission's primary regulatory objective should be to assure the full and nondiscriminatory implementation of the requirements of § 251(c) and the other "wholesale" regulations that are designed to give the ILECs' competitors access to facilities needed to compete at the retail level on nondiscriminatory rates, terms, and conditions. Only *after* the Commission concludes its ongoing review of the rules governing such access – and shores up those rules in response to the ongoing ILEC abuses designed both to impede broadband competition and further insulate voice monopolies from competition – should the Commission consider changes to the retail regulations.

Finally, Part IV demonstrates that deregulation of ILEC broadband services cannot be justified under an approach that ignores market power in pursuit of undefined "regulatory parity" or increased broadband deployment goals. SBC's "regulatory parity" and increased deployment claims run roughshod over the facts, the Telecommunications Act, and dispositive economic distinctions between ILECs and cable companies. SBC's proposed approach of deregulating ILECs without regard to the impact on competition and consumers

would benefit no one but the ILECs. This approach could encourage ILEC broadband deployment – if at all – only at the unacceptable and unlawful cost of reducing broadband and voice competition.

I. WIDELY VARYING COMPETITIVE CONDITIONS AND MULTI-FACETED MARKET POWER CONSIDERATIONS PRECLUDE ANY BLANKET DETERMINATIONS THAT ILECS LACK RELEVANT MARKET POWER IN THE PROVISION OF BROADBAND SERVICES.

The Commission's dominant carrier regulations consist of tariffing, cost support, and related filing requirements that help enforce §§ 201-202 of the Act and their requirements that the rates for common carrier services be just, reasonable, and nondiscriminatory. The regulations require the filing of information that aids the public and the Commission in detecting "price squeezes" and other forms of unreasonable and anticompetitive practices, in assuring that differences in rates for different services reflect cost differences and are not discriminatory, and in assuring that rate levels are just, reasonable, and not excessive.

These regulations apply to any "dominant carrier," which the FCC's regulations define as a carrier that possesses "market power."[9] "Market power," in turn, is defined as the "power to control prices,"[10] that is, "the ability to raise and maintain price above the competitive level without driving away so many customers as to make the increase unprofitable."[11] As the *Notice* states and as the Commission repeatedly has held, a carrier may exercise market power in at least two ways: (1) "by restricting its own output" or (2) "by increasing its rivals' costs or by

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[9] 47 C.F.R. § 61.3(q).

[10] *Id.*

[11] *Policy and Rules Concerning Rates for Competitive Common Carrier Services & Facilities Authorizations Therefor*, Fourth Report & Order, 95 FCC 2d 554, ¶ 8 (1983).

restricting its rivals output through the carriers' control of an essential input, such as access to bottleneck facilities, that its rivals need to offer their services."[12]

It is undisputed that ILECs have market power over virtually all exchange and exchange access services and are thus generally classified as dominant carriers.[13] Indeed, six years after passage of the Telecom Act, the ILECs still provide well in excess of 90% of the exchange and exchange access services, and their local loops, switches, and transport facilities are essential inputs in all but a small fraction of the exchange services that are now offered by CLECs.[14] Moreover, because "incumbent local exchange carriers are generally treated as dominant carriers," the dominant carrier classification applies to all of their services "absent a specific finding to the contrary for a particular market."[15]

The question in this proceeding is whether it would be permissible and appropriate for the Commission to find that ILECs are not dominant with respect to a small subset of their regulated services. Notably, the *Notice* does not propose any definition of the line that distinguishes "broadband" from "narrowband" services. However, the *Notice* provides that, wherever that line is drawn, the Commission will continue dominant carrier regulations for all high-speed broadband services offered under the ILECs' special access tariffs (which can be purchased by end users and ISPs as well as other carriers). The *Notice* thus asks whether some

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[12] *Notice* ¶ 28; *see also Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area*, Second Report and Order, 12 FCC Rcd. 15756 ¶ 83 (1997) ("*LEC Classification Order*").

[13] *Notice* ¶ 5.

[14] Declaration of Robert Willig ¶ 13 ("Willig Decl.") (attached hereto as Attachment A).

[15] *Notice* ¶ 5.

subset of the ILEC high-speed services are offered in discrete and separate markets in which ILECs have no market power, and if so, whether exempting these services from dominant carrier regulations is otherwise reasonable and appropriate. As explained below, it quite plainly is not.

Indeed, this point is underscored by the arguments that have been advanced in the SBC Petition that gives rise to this proceeding. The only way that SBC can argue for a finding of non-dominance is by advancing arguments that are insufficient under the Commission's precedents and that are based solely on its misreading of the *AT&T Reclassification Order*.[16] In SBC's view, "in determining whether a carrier has market power in the provision of a service," the Commission should look to, and mechanically apply, just "four factors": "(1) market share and changes therein; (2) demand elasticity; (3) supply elasticity; and (4) disparities in size resources, financial strength, and cost structures among the participants."[17] SBC then engages in gerrymandering to fabricate a low "market share" for its broadband services. It lumps together broadband services over which it has monopolies with other services that it is currently barred from providing and services for which it faces no competition with services for which it faces some competition. SBC claims that all of these services comprise *national* markets for large business services and mass market services. SBC then applies the other three factors to these gerrymandered markets to contend that ILECs cannot raise prices by restricting *their own* output of broadband services.[18]

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[16] *Motion of AT&T Corp. To Be Reclassified as a Non-Dominant Carrier*, Order, 11 FCC Rcd. 3271 (1995) ("*AT&T Reclassification Order*").

[17] SBC Petition at 14.

[18] *Id*. at 44-54, 56-64.

Even if SBC's claims were otherwise meritorious, however, the Commission has made it explicit that an ILEC's services cannot be found non-dominant based on application of only these four factors to purported national markets.[19] In particular, while the Commission did ultimately apply these four factors in the *AT&T Reclassification Order*, it did so because of factors that are unique to AT&T and its long distance services and that are inapplicable to ILEC services. In particular, the Commission noted that AT&T "no longer own[ed] bottleneck local access facilities," and could therefore have exercised market power only if it could raise prices by unilaterally restricting its own output.[20] Further, AT&T operated nationally; and because it owned no local bottlenecks, it provided the full range of long distance services under competitive conditions that did not materially vary between services, between customer classes, or between locales.[21] Finally, the Commission was not exempting a small subset of AT&T's services from dominant carrier regulations that would remain applicable to the bulk of its services, and there was no risk that reclassification of AT&T as non-dominant would subvert the application of concededly legitimate dominant carrier regulations to other services.

Because very different facts apply to ILECs, a different and much broader market power analysis is required. This analysis has at least three additional aspects.

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[19] *Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area*, Second Report and Order, 12 FCC Rcd 15756, ¶ 98, *passim* (1997) ("*LEC Classification Order*").

[20] *AT&T Reclassification Order* ¶ 32.

[21] *See LEC Classification Order* ¶ 42 (Commission permissibly relied on national share data for AT&T only because there was no "credible evidence suggesting that there is or could be a lack of competitive performance with respect to a particular service or group of services").

Bottleneck Facilities. First, the Commission must assess the significance of the ILECs' control over bottleneck local access facilities. Even if an ILEC could not raise prices by unilaterally restricting its own output, bottleneck facilities give it the ability to exercise market power in myriad other ways. The ILECs can raise their rivals' costs and restrict their rivals' output by denying access to essential inputs and by engaging in cross-subsidization, price squeezes, and discriminatory provisioning.[22] Indeed, it is this control over bottleneck facilities that makes ILECs dominant over exchange and exchange access services generally. The *Notice* acknowledges that the broadband services in question "are often provided over certain of the same facilities as other local exchange and exchange access services."[23] Further, the Commission has elsewhere found that "incumbent LECs . . . have the incentive and ability" to use their control over bottleneck facilities "to discriminate against competitors in the provision of advanced services" and to restrict their output.[24]

Under the Commission's precedents, these facts are virtually dispositive. The Commission has held that "control of bottleneck facilities" is "[a]n important structural characteristic of the marketplace that confers market power upon a firm" and is "prima facie evidence of market power."[25] Here, moreover, it is quite clear that ILECs have in fact exercised

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[22] *Id.* ¶¶ 100, 158; *accord Notice* ¶ 28.

[23] *Id.* ¶ 6.

[24] *Applications of Ameritech Corp., Transferor, and SBC Communications Inc. Transferee*, Memorandum Opinion and Order, 14 FCC Rcd. 14712, ¶ 186 (1999) ("*SBC-Ameritech Merger Order*"); s*ee id*. ¶¶ 196-97.

[25] *Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefor*, First Report & Order, 77 FCC 2d 308 (1979) ¶ 58. Thus, when the Commission first concluded that "AT&T must be treated as dominant," it did so, in part, because it concluded that "many of AT&T's competitors must have access to [AT&T's] network if they (continued …)

market power through their control over bottleneck facilities. As explained below, they have used this bottleneck control to monopolize the provision of intraLATA broadband services that are used by large and small business customers who do not have cable or other "intermodal" alternatives and to prevent any effective competition for residential broadband services in areas where there is no cable modem service.[26]

Local Geographic Markets. Second, to make non-dominance determinations for any ILEC services, the Commission has held that it will not rely on data of an ILECs' "share" of some national aggregation of individual services.[27] Rather, the Commission rigorously defines product and geographic markets using "the most accurate, up-to-date, and generally accepted economic principles relating to market analysis."[28] Thus, the Commission will define the "relevant product market" by asking "whether, if all carriers raised the price of a particular service or group of services, customers would be able to switch to a substitute service offered at a lower price"; the Commission then includes all these substitutes in the product market.[29]

(… continued)

are to succeed." *Id*. ¶ 62. Conversely, when the Commission later reclassified AT&T as non-dominant, it did so, in part, because, "as a result of divestiture, AT&T no longer own[ed] bottleneck local access facilities." *AT&T Reclassification Order ¶ 32.*

[26] The situation is quite unlike the *LEC Classification Order*, in which the Commission engaged in an extensive review of whether the ILECs' control over bottleneck facilities provided the ability to restrict their rivals' output and in which it concluded – based on ten years of experience in the case of independent LECs – that there were sufficient regulatory safeguards in place to minimize the risk of such exercises of power.

[27] *LEC Classification Order* ¶ 25.

[28] *Id*. ¶ 26.

[29] *Id*. ¶ 28.

"With respect to the relevant geographic market," the Commission considers "if all carriers in a specified area raised the price of a particular service or group of services, customers would be able to switch to the same service offered at a lower price in a different area."[30] The Commission has recognized that under this standard, assessments of ILEC market power generally require definitions of telephone markets as *local or point-to-point*, not national. Consumers can use only the services available where their homes and businesses are located, and it is in these discrete local areas where the ILECs can leverage their local monopolies.[31] Under these standards, ILECs could be declared non-dominant across-the-board only if, contrary to fact, there were *no* local geographic markets in which they can exercise market power.

As explained below, the geographic markets that must be assessed in connection with this *Notice* are unquestionably local and point-to-point. "Nationwide determinations of market power are not possible" here because "the competitive constraints on the ILECs' various broadband offerings do vary widely across the relevant local and point-to-point markets as well as across customer classes."[32]

Product Markets and Protection of the Dominant Carrier Regulation of the ILECs' Access Services. Third, because dominant carrier regulation unquestionably remains appropriate for both the ILECs' narrowband services and their high-speed special access services, the dominance determination at issue in this *Notice* is far more "complex" than that

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[30] *Id*.

[31] *Id*. ¶ 65.

[32] Willig Decl. ¶ 10.

posed in prior proceedings.[33] The Commission must assure itself that the "lines" that define any services that are to be carved out from dominant carrier regulation correspond to rigorously defined and discrete product and geographic markets and are economically defensible, rational, and enforceable. Otherwise, the result of the reclassification would be to impair the effective regulation of the concededly dominant narrowband and broadband special access services.

In this regard, any notion that there is a market-based "boundary" between 56 kbps and higher speed exchange services and narrower band services (and all high-speed special access) is patently unsustainable. Among other things, recent technological advances are expected to allow even "narrowband" Internet services provided over the low frequency portion of copper wires to be "always on" and to support data transfer speeds in excess of the 56kps that ILECs claim qualify as "broadband."[34] Further, IP voice telephony, delivered over the "broadband" potion of the local loop is already a reality in the market today.[35] As a result, a non-dominance determination with respect to ILEC broadband services quickly could become a substantial loophole through which the ILECs could avoid regulation of other services that indisputably should remain subject to dominant carrier regulation.

In addition, because the RBOCs control bottlenecks that are essential inputs to the full range of their narrowband and broadband services, the analysis in this proceeding has to take into account that ILECs can "abuse market power . . . across service and market boundaries."[36]

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[33] *Id*.

[34] *Id.* ¶ 16

[35] *Id*.

[36] *Id.* ¶ 12.

For example, because "narrowband and broadband services can be (and are) provided simultaneously over the same copper wires, there must, for example, be careful consideration whether there are economies of scope or complementarities in production or demand that could facilitate market power abuses."[37] Providing both voice and DSL services over the same ILEC-owned loop may be the best, or only, means of profitable entry into these local markets in many areas of the country, and many broadband customers may place a substantial value on obtaining broadband and voice services from the same provider.[38] As a result, changes in the regulatory scheme that make it easier for ILECs to raise their rivals' costs of providing DSL services over network elements will impair the effectiveness of the dominant carrier regulation of the ILECs' voice services – and would also impose significant societal costs by deterring competition by independent LECs for the delivery of local voice services.[39]

Similarly, a decision as to whether to change the regulation of DSL service "would also need to consider whether the ILEC would have the incentive and ability to steer customers away from its DSL service and to its more profitable narrowband services" through cost misallocations or other such behaviors.[40] Regardless of formal market definitions, there can be no question that "broadband" and narrowband services are inextricably linked. For ILECs, both forms of access are provided over the same copper wires and promotion of one service may come at the expense of the other.[41] In this regard, although some consumers may have needs that

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[37] *Id*. ¶ 14.

[38] *Id*.

[39] *Id*.

[40] *Id*. ¶ 15.

[41] *Id*.

only can be met by broadband, that cannot be said of most people considering whether to "upgrade" to higher speed service, and the relative prices of broadband and narrowband clearly are determinative of the choice for many customers.[42]

The best way to address these concerns would be to reject any attempt to treat broadband services as a separate market for purposes of a non-dominance determination if there is any significant potential for consumers to substitute narrowband for broadband services. That would not foreclose the Commission from treating broadband and narrowband as separate markets for other purposes in other contexts.[43] But regardless of how markets are defined, the Commission should assure that any "boundary" it draws is rational, enforceable, and based in economics and technology and does not permit subversion of the dominant carrier regulation of the ILECs' narrowband services. In short, the market power determination "in this context is, of necessity, a multi-faceted analysis that examines each of the many ways in which the services in question and the underlying facilities over which they are provided could be used to impede competition in the relevant geographic areas."[44]

II. ILECs HAVE PERVASIVE MARKET POWER IN THE PROVISION OF BROADBAND SERVICES.

A. Large Business Services.

The ILECs' market power is starkly evident in the provision of data services to

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[42] *Id*.

[43] *See, e.g., Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations by Time Warner Inc. and America Online, Inc., Transferors, to AOL Time Warner Inc., Transferee*, Memorandum Opinion & Order, 16 FCC Rcd 6547, ¶¶ 53-74 (treating broadband and narrowband as separate markets for antitrust purposes).

[44] Willig Decl. ¶ 17.

large business customers. At the outset, it is a misnomer to refer to these services as "broadband" services. The most commonly used of these services is frame relay, yet about half of all frame relay ports are 56 or 64 kbps ports[45] – *i.e.*, on the "narrowband" side of any conceivably defensible speed-based line.[46] Thus, even if it could be demonstrated that exemptions from dominant carrier regulation are warranted for "broadband" services – and, as demonstrated below, it cannot – that would provide no basis for deregulating large business data services.

In any event, SBC's request for an exemption for these services fails even the market-share-driven test that SBC advocates. In the areas where they have been allowed by law to provide such services, ILECs have locked up well over 90% of the business, not the paltry 12% that SBC misleadingly claims. And once the ILECs' continuing and omnipresent control over bottleneck special access facilities is taken into account, the question whether ILECs have market power over the retail large business services which are dependent on the ILECs' provision of these facilities is not even close. The essential nature of these special access facilities gives the ILECs the incentive and ability to leverage their power from the provision of these inputs to the provision of the retail services, as their actual conduct, detailed below, conclusively confirms.

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[45] *See* IDC, U.S. Packet/Cell-Based Services Market Forecast and Analysis, 2000-2005, at 15 (2001).

[46] The Commission has defined "advanced services" as those with data transfer speeds of 200 kbps or higher in both the upstream and downstream direction, and "high-speed" services as those with such transfer speed in at least one direction. *Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996*, Third Report, FCC 02-33, ¶ 7 (Feb. 6, 2002) ("*Third Section 706 Report*").

1. Market Definition. The two primary large business services referred to in the *Notice* are frame relay and asynchronous transfer mode ("ATM"). Both services can be used to connect a customer's data networks (local area networks, or LANs). Frame relay is packet-based, while ATM is cell-based. Together, they have been estimated to have constituted 96.4% of such services provided in 2000 (82.7% for frame relay and 13.7% for ATM), and are predicted to account for 99.7% in 2005 (81.1% for frame relay and 18.6% for ATM).[47]

Other packet/cell-based services include X.25 and Switched Multimegabit Data Service (SMDS). Both are relatively insignificant, and both are expected to decline rapidly in the next few years.[48] X.25 is an extremely slow service (again, not a broadband service), and it is declining as customers migrate toward LAN-based applications.[49] SMDS is offered primarily by local carriers and is essentially a local service. It is being phased out, and in 2000 Bell Atlantic was the only carrier actively marketing it.[50] Gigabit Ethernet (which is not reflected in the share figures above) is a service that is just being introduced for customers that need extremely high bandwidth connections.[51]

The only two services analyzed by SBC's witnesses Crandall and Sidak in their discussion of "larger-business advanced services" are frame relay and ATM. It is reasonable to treat these two services as in the same product market. For many customers, the two services are

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[47] IDC, U.S. Packet/Cell-Based Services Market Forecast and Analysis, 2000-2005, at 5-6 (2001).

[48] *Id.* at 1-2.

[49] *Id.* at 81, 84.

[50] *Id*. at 118.

[51] Willig Decl. ¶ 51.

reasonable substitutes; they are priced similarly; and they clearly compete with one another.[52] There is no need to decide whether SMDS, X.25, or Ethernet services are also in this same market. The pertinent question is whether these less economically significant services should be regulated in the same manner as frame relay and ATM, and there is no apparent reason why they should not be.[53]

The relevant geographic markets are point-to-point markets (or, more precisely, multi-point markets) defined by the locations that the customers of these services seek to link. As the Commission explained in the *LEC Classification Order*,[54] customers in Miami generally purchase long distance calling plans originating in Miami; for such customers, calling plans originating in Los Angeles are not a viable substitute.[55] Likewise, a large business that wants to link its offices in Dallas, Houston, and Austin must turn to suppliers that offer frame relay and ATM services in those areas.[56]

Of course, if there were no material competitive differences from one multi-point market to the next, a collective analysis of all such markets could be appropriate.[57] But the

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[52] *Id.* ¶ 52.

[53] *Id.* ¶ 53. The *Notice* also refers to Remote Local Area Network ("RLAN"). *See Notice* ¶ 22. This is a purely local service, typically used to connect a home or small office to an enterprise's LAN. For example, a DSL line that is connected to a LAN (rather than an Internet Service Provider) would be classified as RLAN service. RLAN is not in the same product market as frame relay or ATM, which are commonly used to connect several LANs.

[54] *LEC Classification Order* ¶ 65.

[55] *Id*.

[56] Willig Decl. ¶ 55.

[57] *See LEC Classification Order* ¶ 66 (noting that all point-to-point long distance services would be analyzed collectively "unless there is credible evidence indicating that there is or could be a lack of competition in a particular point-to-point market").

Commission has already recognized in its *Pricing Flexibility Orders* that competition in the provision of the "last mile" high-capacity loops and transport that are an essential input in providing retail large business data services may vary materially from one locale to the next.[58] And, as the *Notice* recognizes, retail market power plainly can turn on the presence or absence of market power over essential inputs to the retail service.[59] Thus, the Commission could not rationally grant SBC's request for a national share-based across-the-board business services exemption. Instead, SBC would have to demonstrate on a market-by-market basis that its high-capacity loops and transport facilities do not give it market power in the provision of retail services. As detailed below, SBC could not possibly make those showings. Indeed, the evidence from the locales in which the ILEC's special access service face the most competition overwhelmingly demonstrates that there are *no* locales in which the ILEC's special access services are no longer bottlenecks, and that the Commission therefore could – and should – categorically reject the ILECs' pleas for large business services exemptions from dominant carrier regulation.[60]

2. The ILECs' Dominant Market Share. SBC contends that its lack of market power is conclusively demonstrated by the fact that it provides only 12-16% of the frame relay and ATM services provided in its region. In fact, the very data and third party sources

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[58] *Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers, Petition of U.S. West Communications, Inc., for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA,* Fifth Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd. 14221, ¶¶ 71-76 (1999).

[59] *See Notice* ¶¶ 28-29.

[60] Willig Decl. ¶¶ 67-68.

upon which SBC purports to base its remarkably misleading share figures only confirm that SBC can – and does – leverage its bottleneck control over the underlying facilities into absolute dominance of any retail large business data services for which it is allowed to compete.

The only reason why the ILECs do not provide a particularly large share of the large business services on a national basis is that they are still largely confined by § 271 to providing such services on an intraLATA or "local" basis. Thus looking at national or regional shares is not a meaningful way in which to examine the extent of the ILECs' market power. Instead, the focus from a geographic perspective must be on the markets where the ILECs' true power has been allowed to manifest itself. These are the multi-point frame relay and ATM services provided within LATAs, which the ILECs dominate almost to the exclusion of other carriers.

When the legal restrictions on the market presence of the RBOCs are appropriately taken into account, it is clear under even the market-share driven test proposed by SBC, that the ILECs could not justify any across-the-board finding of non-dominance in the provision of data services to large businesses. Although SBC and its witnesses Crandall and Sidak never mention it, the data from the IDC reports on which they rely establishes that a customer desiring an ATM network that crosses LATA boundaries can choose among a number of carriers, none of which has more than a 30% share.[61] But if the customer wants a "local" ATM network, it would (as shown below) generally confront a situation in which the RBOC in that area controls 90 to 100% of the service:

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[61] *See* IDC, U.S. Packet/Cell-Based Services Market Forecast and Analysis, 2000-2005, at 57 (2001).

Share of Revenues (Aggregated Nationally) for "Local" Large Business Data Services in 2000

Carrier	Frame Relay Share[62]	ATM Share[63]
Bell Atlantic	23.8%	27.6%
SBC	24.8%	41.2%
BellSouth	20.5%	8.7%
US West	16.7%	11.0%
GTE	6.0%	7.7%
Sprint	3.0%	------
MCI WorldCom	2.2%	1.5%
AT&T	0.9%	1.2%
Other CLECs	2.1%	1.1%
Total incumbent LEC	91.8%	96.2%

What these data obviously reflect is that, within its service area, each ILEC has a *de facto* monopoly over the provision of both frame relay and ATM services wherever it has been allowed to compete.[64] And according to IDC, this dominance is not eroding: absent much-needed regulatory intervention to address the underlying bottleneck problem, the RBOCs will continue to dominate the provision of "local" frame relay markets.[65]

As interLATA restrictions are lifted, the dominant carrier and other regulations described below are the only things standing in the way of the ILECs' plan to expand their dominance, first regionally and then nationally.[66] The ILECs will still control essential

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[62] *Id.* at 34.

[63] *Id.* at 69.

[64] Willig Decl. ¶ 68.

[65] IDC, U.S. Packet/Cell-Based Services Market Forecast and Analysis, 2000-2005, at 28, 34-35 (2001).

[66] "The RBOCs will most likely target the broader regional markets in their current operating (continued …)

bottleneck facilities and as a result will still be able to gain an unfair competitive advantage over their rivals though discriminatory pricing and other discriminatory conduct, just (as discussed below) they do today in the provision of the intraLATA services they are allowed to provide.

3. The ILECs' Control of Bottleneck Facilities. The reason that the ILECs have such a high share of the large business data services in areas where they have been allowed to enter is because of the ways in which they can use their control over bottleneck special access services to unfairly disadvantage their rivals. The ILECs have exercised this power by charging their large business service rivals supracompetitive prices for special access (and thereby creating a classic price squeeze), by providing rivals with poorer quality interconnections, and by imposing unnecessary delays. As the Commission has long recognized, such discriminatory conduct is direct evidence of market power.[67]

(*a*) *The ILEC's dominance over special access.* ILECs are clearly dominant in the provision of large-business services inputs to other carriers, because fundamental economics (and the Commission's own "use limitations" regulations) force other carriers to rely upon the ILECs' special access services.[68] Although the *Notice* properly recognizes that non-

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(… continued)

regions and will initially relay on network-to-network interface agreements for nationwide coverage." *Id.* at 23.

[67] *Notice* ¶ 29; *SBC-Ameritech Merger Order* ¶107.

[68] Although special access services use the very same loops and transport facilities that are provided as unbundled network elements, CLECs serving larger business customers must generally secure access to ILEC loops, transport, and combinations thereof via special access tariffs. The principal reason for this predicament is the Commission's decision to permit ILECs to limit the manner in which CLECs may use combinations of the loop and transport elements. *See* Reply Comments of AT&T, *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98 (Apr. 30, 2001).

dominant treatment of special access services should not even be considered at this time, the ILECs' special access dominance just as plainly cannot be ignored in assessing the claims of non-dominance for the large business services that are expressly within the scope of this proceeding. To the contrary, it is the ILECs' dominance in the provision of these wholesale services which is the direct source of their dominance over retail markets.

As much as AT&T and other competitive carriers would prefer to self-provide last-mile facilities, or obtain them from non-incumbent sources, the ILEC remains the only source for these facilities in the overwhelming majority of situations. As the Commission recognized in the *UNE Remand Order*, self-provisioning is not a viable alternative because "replicat[ion of] an incumbent's vast and ubiquitous network would be prohibitively expensive and delay competitive entry."[69] The ILECs have ubiquitous transport facilities that connect

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[69] *UNE Remand Order* ¶ 182; *see also id.* ¶ 321 ("[S]elf-provisioned transport, or transport from non-incumbent LEC sources, is not sufficiently available as a practical, economic and operational matter."). Carriers have echoed the same sentiment. *See, e.g.*, Comments of Sprint Corporation, *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 5 (Jan. 22, 2002) (noting that it "continues to rely upon the ILECs for approximately 93% of its total special access needs despite aggressive attempts to self-supply and to switch to facilities offered by alternative access vendors (AAVs) whenever feasible"); Comments of WorldCom, Inc., *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 5 (Jan. 22, 2002) (explaining that "[i]n the past year, approximately 90 percent of . . . [its] off-net special access circuit needs were provisioned by the incumbent LECs, even though it is . . . [its] policy to use the local facilities of WorldCom or other competitive carriers whenever such facilities are available"); Comments of VoiceStream Wireless Corporation, *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 5 (Jan. 22, 2002) ("CMRS carriers remain heavily dependent on the special access facilities provided by the ILECs."); Reply Comments of Sprint Corporation, *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 2 (Feb. 12, 2002) ("There is virtual unanimity among commenting IXCs, CLECs, CMRS providers, and large end users that ILECs remain dominant in the provision of special access services"); Reply Comments of Cable & Wireless USA, Inc., *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 2-11 (Feb. 12, 2002).

14,000 Local Serving Offices and over 220 million loops.[70] No CLEC or IXC can hope to replicate this network. This is true not only for low capacity facilities (DS1 or below) but also high capacity facilities (DS3 or above).[71]

SBC's assertion in its petition that "SBC's competitors often do not use SBC local access facilities"[72] is demonstrably false. In SBC's territory and throughout the nation, AT&T and other competitors remain heavily dependent upon the ILECs for both interoffice transport facilities and local loops. Today, for the "backbone" portion of AT&T's local network, AT&T almost never self-provides DS1 transport and self-provides DS3 transport only a small minority of the time. Likewise, for the local loops used to provide connectivity between the customer's premise and the local serving office, AT&T provides only a tiny fraction of its DS1s entirely on its own network.[73] The remaining service is provided almost exclusively by utilizing the facilities of the ILECs.[74]

The recent ruling of the New York Public Service Commission ("NYPSC") that Verizon remains the "dominant" provider of special access services in *all* of that state, including lower Manhattan – the area that is generally regarded as the *most* competitive in the United States – is compelling proof of the ILECs' continuing market power.[75] The NYPSC carefully

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[70] *See* Federal-State Joint Board, *Universal Service Monitoring Report*, Tables 10.1, 10.2 (Oct. 2001).

[71] *See* Declaration of Anthony Fea and William Taggart ¶ 5 ("Fea/Taggart Decl.") (attached hereto as Attachment B).

[72] SBC Petition at 73

[73] Fea/Taggart Decl. ¶ 6.

[74] *Id.*; Declaration of Alan Benway ¶¶ 6 ("Benway Decl.") (attached hereto as Attachment C).

[75] *See Proceeding on Motion of the Commission to Investigate Methods to Improve and Maintain*
(continued …)

analyzed a detailed record regarding route miles of fiber, numbers of buildings passed and especially numbers of buildings actually *connected* to ILEC competitors, and concluded that "Verizon's combined market share data demonstrates its continued dominance in *all* geographic areas. . . . In [New York City], for example, Verizon has 8,311 miles of fiber compared to a few hundred for most competing carriers; Verizon has 7,364 buildings on a fiber network compared to less than 1,000 for most competing carriers."[76] Verizon's own data show that "a maximum of 900 buildings [are] served by individual competitors' fiber facilities," but New York City has "775,000 buildings in the entire city, over 220,000 of which are mixed use, commercial, industrial, or public institutions."[77] The NYPSC further concluded that claims regarding "buildings passed" by competitors' facilities were virtually meaningless as evidence of a competitive market because "the data do not reflect how often fiber actually enters those buildings."[78] "Because competitors rely on Verizon's facilities, particularly its local loops," the

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High Quality Special Services Performance by Verizon New York Inc., Opinion and Order Modifying Special Services Guidelines for Verizon New York Inc., Conforming Tariff, and Requiring Additional Performance Reporting, NY PSC Case 00-C-2051, at 6 (June 15, 2001) ("*NYPSC June Special Services Order*"). What the NYPSC calls special services are "known as 'special access' when provided pursuant to federal tariffs. Special access services are provided pursuant to Federal Tariff if the customer advises that more that 10% of the traffic will be inter-state, regardless of where the facilities to serve the traffic are located. For reporting purposes, all special services are addressed by the Commission's Special Services Guidelines." *Proceeding on Motion of the Commission to Investigate Methods to Improve and Maintain High Quality Special Services by Verizon New York Inc., Order Denying Petitions for Rehearing and Clarifying Applicability of Special Services Guidelines*, NY PSC Case 00-C-2051, at 1 (Dec. 20, 2001) ("*NYPSC December Special Services Order*").

[76] *NYPSC June Special Services Order* at 7.

[77] *Id*. at 7-8 (citing to Land Use Facts, Department of City Planning).

[78] *Id*. at 9.

NYPSC found, "Verizon represents a bottleneck to the development of a healthy, competitive market for Special Services."[79]

If CLECs are still so reliant on ILEC-supplied facilities in New York City, there is no reason to believe that ILECs lack market power anywhere in the country. Certainly SBC and the other ILECs have not demonstrated that they lack this market power, either nationally or in any of the areas they serve. Nor will this situation change in the foreseeable future. In most cases, it is simply not feasible for competitors to build facilities directly to the end user's premises.[80]

Contrary to SBC's claim,[81] ILECs do not lack market power in areas in which they have obtained special access pricing flexibility. In its *Pricing Flexibility Order* the Commission expressly declined to find that the provision of loops and transport is sufficiently competitive to consider the ILECs non-dominant in the provision of special access services,[82] and the D.C. Circuit expressly relied upon that finding in affirming the Commission's order.[83] The new pricing flexibility rules were intended only to permit ILECs to *respond* to emerging –

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[79] *Id*.

[80] New network construction typically requires cooperation from localities, other carriers, and building owners and can take months or even years to complete. Most end users are unwilling to deal with these delays. Even in those limited instances in which it is economically feasible to deploy facilities, CLECs face a number of hurdles that frustrate the self-deployment of facilities, including the need to obtain access to rights-of-way and buildings, existing ILEC volume or term commitments, exhaustion of collocation capacity, and long distances between points of presence and ILECs' end offices. *See* Fea/Taggart Decl. ¶¶ 30-31.

[81] *See* SBC Petition at 73.

[82] *Pricing Flexibility Order* ¶ 151, n.372

[83] *See WorldCom, Inc.* v. *FCC*, 238 F.3d 449, 460 (D.C. Cir. 2001) ("[T]he FCC did not engage in the thorough competition analysis" that would be expected in "non-dominance proceedings").

but not yet established – competition. That is presumably why the Commission expressly required ILECs to continue to tariff special access services,[84] and why the Court found the Commission's commitment to appropriate investigation of those tariffs so important. And the ILECs' response to pricing flexibility – maintaining or increasing special access rates, rather than lowering them to meet competition[85] – removes any possible basis for resting any market power determinations on the outcome of pricing flexibility proceedings (and also suggests that the Commission should take a hard look at its pricing flexibility criteria, which, at least so far, appear almost certainly to have harmed, rather than helped, competition and consumers).

(*b*) *The ILECs' abuse of their special access dominance to monopolize the provision of data services to large businesses.* The *Notice* properly recognizes the economic commonplace that control over bottleneck facilities that are essential to the provision of a retail service can give the owner of those facilities both the incentive and ability, through

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[84] *See id*. ¶151.

[85] Bell South filed Transmittal No. 608, effective November 1, 2001, increasing Special Access rates for DS3 and DS1 services in MSAs with Phase II pricing flexibility. Verizon filed Transmittal No. 134, effective January 5, 2002, increasing Special Access rates for DS1 services in MSAs with Phase II pricing flexibility. *See also* Comments of the Ad Hoc Telecommunications Users Committee, *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 2 (Jan. 22, 2002) ("Rates are *higher* in markets where the Commission has granted ILECs Phase II pricing flexibility than in markets subject to price cap regulation."); *id.* at 4-5 ("[O]ur analysis revealed no instance of lower prices for generally available services in the MSAs to which Phase II pricing flexibility applies."); *id.* at 6 ("In downtown Manhattan, for example, the price for DS1 special access between two locations served by the same wire center would be $387.76, more than $30.00 (close to 10%) higher than the rates that would be in effect if the Commission had not granted Phase II pricing flexibility to NYNEX for New York City."); Comments of Sprint Corporation, *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 5 (Jan. 22, 2002) ("Sprint would note that ILECs that have been granted special access pricing flexibility have done little with such regulatory relief other than to raise their special access prices – hardly the behavior of carriers facing robust competition.").

discrimination that raises rivals' costs, to gain market power in the provision of the retail service.[86] Such discrimination can take the form of access prices that are higher than the costs that the bottleneck owner incurs (and thus create a "price squeeze" that makes it impossible for retail rivals to turn a profit) or non-price discrimination, such as degraded quality or provisioning delays. Neither the general theory, nor its clear applicability to ILECs, is subject to any serious debate.[87] And although the ILECs have in the past argued (not very convincingly) that circumstances particular to a given service may dampen their incentives to behave anticompetitively or reduce their ability to do so, no such argument is possible here. SBC and other ILECs have, in fact, used both price and non-price discrimination to dominate the retail provision of data services to large business customers wherever they have been allowed to provide those services.[88] Monopoly leveraging is not a mere theoretical concern in this context, but a real world problem that could only be exacerbated by the deregulation that SBC and others seek in this proceeding.

The evidence of both the existence and effectiveness of the ILECs' price squeeze of retail data service rivals, for example, could hardly be more stark. Although the situation varies somewhat from ILEC to ILEC, there are numerous geographic areas where the ILEC special access charges incurred by AT&T are higher than the *retail* price the ILEC is charging

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[86] *Notice* ¶ 29.

[87] *See, e.g., Non-Accounting Safeguards Notice* ¶ 14; *see also* Willig Decl ¶¶ 70-76.

[88] *Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1935 as Amended*, Notice of Proposed Rulemaking, 11 FCC Rcd. 18877, ¶ 14 (1996) ("*Non-Accounting Safeguards Notice*").

customers directly for its intraLATA frame relay or ATM ports.[89] In fact, in an analysis undertaken by AT&T, this was true in more than *half* of the areas studied.[90] These access costs go directly into the cost that AT&T must charge its customers (and, often make up the majority of the relevant costs), and make it impossible for AT&T to compete. In some areas, the rates exceed the price that AT&T considered necessary to provide a competitive offering by as much as 150%.[91]

This is a classic price squeeze, and it already has had a devastating effect on competition. After the passage of the Telecommunications Act of 1996, AT&T undertook an aggressive effort to enter the intraLATA business services market. But because its costs of providing service are so severely inflated by the ILEC's anticompetitive pricing of special access, AT&T has been forced to scale back its efforts (with the exception of the very limited number of customers who can be reached by AT&T's own local facilities).[92] This abandonment is directly reflected in the market share data, and it is compelling evidence not only of the ILECs' dominance in the provision of intraLATA services, but of their incentive and ability to expand that dominance as they obtain interLATA authorizations.[93]

Furthermore, contrary to SBC's claim, the high demand elasticity of large business services cuts *against* a non-dominance finding here. Because of the high elasticity of demand, even a small artificial cost advantage facilitated through price squeeze will be enough to

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[89] Benway Decl. ¶ 13.

[90] *Id*.

[91] *Id*.

[92] *Id*. at ¶¶ 17-18.

[93] Willig Decl. ¶¶ 67-69.

win the customer. And, although existing regulation is not alone sufficient to prevent the ILECs from leveraging their special access market power into the market for large business services – only truly forward-looking cost-based access charges could accomplish that – the tariff filing requirements at least provide a means of detecting anticompetitive price squeeze behavior.[94]

The ILECs' non-price discrimination is also well documented and further confirms the ILECs' incentives and ability to use their special access bottlenecks to gain market power in the provision of data services to large businesses.[95] As AT&T and many other commenters recently demonstrated in the *Performance Measurement and Standards for Interstate Special Access Services* docket, poor quality, delays, and other discrimination in favor of the ILECs, their affiliates and their retail customers is widespread and debilitating.[96]

The comments by the New York State Department of Public Service in that docket illustrate the magnitude of the problem and the reality that the ILECs' "uneven

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[94] *Id.* ¶ 76.

[95] *See Notice* ¶ 29; *SBC-Ameritech Merger Order* ¶ 107*; see also* Willig Decl. ¶ 70 ("Furthermore, they will have both the incentive and the ability to discriminate against competing carriers in providing the inputs necessary to offer broadband services.").

[96] *See* Comments of AT&T, *Performance Measurements and Standards for Interstate Special Access Services et al.*, CC Docket No. 01-321, at 13-17 (Jan. 22, 2002); *see also* Comments of Cablevision Lightpath, *Performance Measurements and Standards for Interstate Special Access Services* et al, CC Docket No. 01-321, at 3 (Jan. 22, 2002); Aff. of Richard Johnson at 2, appended to Comments of VoiceStream Wireless, *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, (Jan. 22, 2002); Comments of WorldCom, Inc. *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 14 (Jan. 22, 2002); Reply Comments of Ad Hoc Telecommunications Users Committee, *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 2-3, 13-15 (Feb. 12, 2002); Reply Comments of Association of Communications Enterprises, *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 2-9 (Feb. 12, 2002); Comments of Cable & Wireless USA, Inc., *In the Matters of Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 1-2, 12 (Feb. 12, 2002).

performance threatens to undermine competition" in all services that rely upon ILEC special access.[97] As just one example, the New York Department reported that "Verizon, on average, met only 74 [percent] of its appointments on carrier service requests, but met 94 [percent] of its retail customer appointments."[98] Other state commissions have made similar findings.[99] End user customers concur. The Ad Hoc Telecommunications Users Committee has concluded that even the most competitive markets have done little to constrain the ILECs' discriminatory behavior toward carriers or end user customers, the ultimate beneficiaries of improved ILEC service.[100]

AT&T's data indicate that ILECs consistently failed to provision AT&T's DS-1 orders in a timely manner more than 10% of the time.[101] And, disturbingly, the data reflect a

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[97] Comments of the New York State Department of Public Service, *Performance Measurements and Standards for Interstate Special Access Services, et al*., CC Docket No. 01-321, at 2-3 (Jan. 18, 2002).

[98] *Id*. at 3.

[99] *Complaint of AT&T Communications of the Midwest, Inc. Against U S WEST Communications, Inc., Regarding Access Service*, MPUC Docket No. P-421/C-99-1183, 2000 Minn. PUC LEXIS 53, *34 (Aug. 15, 2000); *AT&T Communications of the Mountain States, Inc. Complainant, v. U S WEST Communications, Inc., Respondent*, CPUC Docket No. 99F-404T, Decision No. R00-128, at II. D, F, G (Feb. 7, 2000) ("AT&T has experienced regular, frequent, widespread, and ongoing delays in obtaining access . . . When U S WEST does not meet its dates for the provision of service, it works a hardship on AT&T as well as AT&T customers . . . On a region-wide, multi-state basis, U S WEST has provisioned DS1s and DS0s to AT&T on a wholesale basis after a longer interval than it provided those same services to other wholesale customers".).

[100] Comments of the Ad Hoc Telecommunications Users Committee, *Performance Mesurements and Standards for Interstate Access Services*, CC Docket No. 01-321, at 4 (Jan. 22, 2002); *See also* Comments of American Petroleum Institute, *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 4 (Jan. 22, 2002) (concluding that ILEC delays in provisioning special access service ultimately prevent end users from switching from one carrier to another).

[101] *See* Decl. of Maureen A. Swift, Reply Comments of AT&T, *Performance Measurements and*

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downward trend in on-time performance. Further, over the five-year period covered in AT&T's analysis, the ILEC-provisioned DS-1 failure-frequency rate was as high as 23% and was *always* above 10% – and restoration times remain unacceptable.[102] In short, the ILECs' special access performance is abysmal and worsening. In the face of high demand elasticity, such severe price and non-price discrimination all but guarantees continued ILEC dominance in the provision of any retail data services they are allowed to offer.

B. Mass Market Services.

Although SBC's Petition is remarkably vague on the subject, the "mass market" broadband services for which the ILECs seek dominant carrier exemptions apparently encompass: (1) both DSL-based telecommunications services that ILECs provide to ISPs and other carriers and bundles of DSL and ISP services that ILECs market to consumers; (2) both services marketed to residential consumers and services marketed to businesses; and (3) both ILEC services provided in dense urban areas where cable (and in some cases, wireless and other) broadband services are available and services provided in areas where DSL is currently the only available broadband choice. SBC contends that the mere existence of intermodal competition from cable provides a rational basis to conclude that ILECs lack market power over all such services everywhere. As detailed below, however, any reasoned analysis must conclude that the

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(… continued)

Standards for Interstate Special Access Services, et al., CC Docket No. 01-321, ¶¶ 10-12 (Feb. 12, 2002) ("Swift Declaration") (attached hereto as Attachment D). The Swift Declaration reports national average performance because AT&T's agreements with individual ILECs preclude it from providing data on an individual basis. *See id.* 9.

[102] Indeed, it takes ILECs more than three hours to restore failed circuits almost 30% of the time. *See id.* ¶ 11. Customer satisfaction is clearly linked to a carrier's ability to avoid outages and, in the event an outage occurs, to restore service quickly.

relevant competitive conditions vary widely, that service, area, and customer class-specific inquiries are therefore required, and that when such inquiries are conducted they reveal multi-faceted and pervasive ILEC market power. Although some ILECs may, in future petitions, be able to demonstrate that dominant carrier regulation is no longer needed with respect to some broadband offerings provided to some classes of customers in some areas, no ILEC has yet done so. SBC's Petition, in particular, falls far short of the required showing that market power is lacking.

1. Services Provided at "Retail" to Consumers and Small Businesses. According to SBC, cable companies, collectively, have more residential broadband subscribers than ILECs, collectively. Thus, SBC concludes, ILECs lack market power in the *entire* retail mass-market business, for residences and businesses alike, throughout the entire nation.[103] The marketplace realities are quite different. Contrary to SBC's claim, ILEC retail mass market broadband services do not uniformly face intermodal competition, and thus there is no possible basis upon which an across-the-board exemption could be justified. Moreover, there is substantial direct evidence that ILECs not only can but have profitably raised prices and thus retain market power notwithstanding intermodal competition from cable. It is likewise clear that ILECs have both the incentive and ability anticompetitively to structure their retail and wholesale broadband offerings in order to maintain and enhance their narrowband monopolies and to deter narrowband entry.

(a) Market definition. The boundaries of the geographic market are straightforward. The relevant markets are local because consumers in a given community can

[103] SBC Petition at 42 ("[T]his market share data should be dispositive.").

buy broadband (or narrowband) services only from providers that offer those services in that community. "[T]he only way to obtain different choices is to move."[104]

Delineating the contours of the product market is more difficult. At the outset, it is important to recognize that, unlike cable modem services, the xDSL services that RBOCs provide today (and the RBOCs provide almost *all* xDSL services today) are *not* Internet access services. Rather, they are xDSL-based telecommunications services that require the purchase of a separate ISP service (which generally is provided by a third party) to allow for Internet access. The Commission has consistently recognized that such telecommunications services are in separate product markets from Internet access services.[105] That said, it is nonetheless useful to examine competition between cable modem services and DSL-based Internet access services, because the RBOCs virtually always market their DSL telecommunications services bundled with ISP services (that they claim are being provided by third parties).

The *Notice* observes that the Commission has, for antitrust purposes, previously identified a broadband market (which includes cable and DSL) as being separate from the narrowband market.[106] Irrespective of whether broadband and narrowband should be considered separate under the antitrust laws, however, there is overwhelming evidence (some of it

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[104] *See, e.g., Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations by Time Warner Inc. and America Online, Inc., Transferors, to AOL Time Warner Inc., Transferees*, Memorandum Opinion and Order, 16 FCC Rcd. 6547, ¶ 74 (2001) ("The relevant geographic markets for residential high-speed Internet access services are local.").

[105] *See, e.g., SBC-Ameritech Order* ¶ 249.

[106] *See Notice* ¶ 26 (citing *Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations by Time Warner Inc. and America Online, Inc., Transferors, to AOL Time Warner Inc., Transferee*, Memorandum Opinion & Order, 16 FCC Rcd 6547, 6568-78, ¶¶ 53-74).

recognized by SBC's own economists) that the two offerings are "reasonably substitutable services,"[107] and that the ILECs' narrowband dominance (and the incentives it creates) must therefore be considered to reach meaningful conclusions about ILEC market power in the provision of broadband services.

As Professor Willig explains in detail, "there is now, and will continue to be for the foreseeable future, a great deal of demand cross-elasticity and opportunities for substitution between the two modes of Internet access."[108] A survey from the Strategis Group[109] and the very econometric study cited by SBC's economists[110] further reinforce this conclusion. Although *some* consumers may have a need for speed that can be met only by broadband, that is not true of most people (who use the Internet primarily for e-mail, instant messaging, and shopping). As the Yankee Group observed, "broadband has yet to be defined by users in terms of the applications or services that high-speed access enables."[111] Narrowband and broadband are available at similar prices, even following the DSL price increases by SBC and other ILECs discussed below.[112] Finally, it simply cannot be dispositive that broadband offers "always-on" service

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[107] *Notice* ¶ 18.

[108] Willig Decl. ¶ 123.

[109] *See* Information Technology Association of America, *Building a Positive Competitive Broadband Agenda*, p. 10 (Oct. 2001) (presenting data from Strategis Group), available at http://www.positivelybroadband.com.

[110] *See* Paul Rappaport, Donald J. Kridel, Lester D. Taylor, Kevin Duffy-Deno, *Residential Demand for Access to the Internet*, University of Arizona Working Paper, at 19 (Spring 2001).

[111] Yankee Group Press Release, *Streaming Music, Video Are Not Pulling in Broadband Subscribers, but Offering Secondary Benefit* (Oct. 22, 2001) ("Less than 2% of those surveyed cited listening to music online, watching video, or playing games as either a primary or secondary reason for subscribing to high-speed access services.").

[112] When the Commission examined retail prices, it found that the monthly cost of broadband (continued …)

because a 56 kbps always-on service is expected to be available soon.[113]

In the end, however, it matters little whether the Commission formally defines the relevant market to include narrowband, so long as the ultimate market power analysis properly accounts for the important interrelationships between broadband and narrowband, as well as the stark evidence that the ILECs' narrowband monopolies have played a vital role in giving them the incentive and ability to exercise market power by raising prices profitably – notwithstanding the existence of nascent intermodal competition.

(b) Market power. SBC has not come close to providing such proof. Indeed, in addressing market share, SBC relies solely on the single fact that "competitors have captured two-thirds of the broadband Internet access market."[114] This national number is utterly unhelpful in assessing the level of competition for particular customer classes or for various local markets, which (as shown below) exhibit wide variation in competitive activity.

For starters, there is almost no intermodal competition for small-business

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(… continued)

Internet access via cable modem is *exactly the same* as the monthly cost of narrowband Internet access, and the "total first-year costs" were actually lower with the cable modem. *See Inquiry Concerning the Deployment of Advanced Communications Capability to All Americans in a Reasonable and Timely Fashion*, Report 14 FCC Rcd. 2398, ¶ 87 & Chart 3 (1999). And despite recent broadband rate increases, the price differences remain fairly insubstantial. *See* Forrester Research, Inc., *Sizing US Consumer Telecom* (Jan. 2002), at. 5 ("For consumers who maintain a second phone line for dial-up access to the Internet, the additional cost of moving to broadband is less than $10."). In any event, the marginal price difference cannot be viewed as evidence that narrowband and broadband are distinct markets. Certainly, neither SBC nor anyone else contends that faster DSL connections are in a separate market from slower DSL connections, even though the prices may vary from $49.95 per month to $79.95 per month. *See, e.g.*, Verizon Pricing and Packages, www22.verizon.com/foryourhome/dsl/order/NLF_vzolproductsprequalify.asp (downloaded Feb. 7, 2002).

[113] Forrester Research, Inc., *Sizing US Consumer Telecom*, at 10 (Jan. 2002).

[114] SBC Petition at 41.

customers. As Professor Willig observes, "[f]ew businesses are served by cable."[115] "For the great majority, their only real broadband choice is DSL."[116] "[C]able doesn't really compete in the small business market;"[117] rather, "[i]t's really DSL's game to win or lose."[118] Furthermore, matters are not expected to improve. As Cahners In-Stat Group explains, cable providers' current "lack of presence in the business market will limit cable modem deployments in the long run."[119] As a result, "[c]able modem service penetration of businesses will remain modest for the next five years. In North America today, businesses only account for 5% of total subscribers. By 2005, this number will rise to only 10% of total subscribers."[120] In short, there is no significant intermodal competition to constrain the pricing of the DSL, T1, ISDN or other high-speed data services that ILECs market to business customers.

But the lack of full intermodal competition extends to residential customers as

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[115] Willig Decl. ¶ 20.

[116] *Id*.

[117] *See Cable Modems Retain Lead But DSL is Growing Faster*, *Communications Daily* (Aug. 2, 2000) (quoting president of Broadband Intelligence)

[118] *Id*.; *see also* Communications Daily (Jan. 31, 2002) (reporting that AT&T's cable plant does not extend to business setting); Communications Daily (Jan. 18, 2002) (reporting that Kansas Corporation Commission refused to reconsider its denial of Southwestern Bell Telephone's petition for rate deregulation of its T-1 high-speed digital service and primary rate ISDN service as fully competitive); *compare* Cahners In-Stat Group, *Despite Service Provider Pratfalls, Cable Modem Subscriber Growth Remains Robust*, at 19 (Dec. 1, 2001) (370,000 cable subscriptions by North American businesses) *with* Cahners In-Stat Group, *U.S. Residential DSL Continues to Grow Despite Market Turmoil*, at 38 (Oct. 1, 2001) (1,035,225 DSL subscriptions by U.S. businesses).

[119] *Id.* at 31.

[120] Cahners In-Stat Group, *Despite Service Provider Pratfalls, Cable Modem Subscriber Growth Remains Robust*, at 1 (Dec. 1, 2001); *see also id.* at 12 ("[B]usiness customers in the United States predictably prefer digital subscriber line and T-1 services to fulfill their broadband communications needs").

well. As the Commission has recognized, what is true "for any technology" is particularly true for broadband, a technology in the early stages of development: Deployment "is not uniform across the nation."[121] About 40% of all U.S. zip codes have only a single high-speed service provider or no high-speed service provider at all.[122] And in some residential areas, cable service is not available to anyone.[123] Moreover, "publicly available information indicates that cable systems capable of providing cable modem service tend to be located in the most densely populated areas, especially in the East, the Midwest, and on the West Coast," and that cable modem service is available to only 70% of U.S. homes[124] Consequently, many consumers simply do not have a cable choice at this time. Nor have wireless or satellite services yet filled the gap. High-speed wireless services are today limited to a small subset of even the most urban areas, and leading providers have recently scaled back their entry plans.[125] And the high-speed satellite services that have recently been rolled out have experienced technical problems, and are

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[121] *Inquiry Concerning the Development of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996,* Second Report, 15 FCC Rcd 20913, ¶ 1 (2000) ("Second Section 706 Report").

[122] *See Third Section 706 Report,* Appendix C, Table 9.

[123] *See id.*

[124] *Id.* ¶ 46; *see also id.* ¶ 35 ("Our data suggest that there is a great disparity in high-speed subscribership at different population densities . . . ."); *id.* ¶ 109 ("[T]here continues to be a significant disparity in access to advanced services between those living in rural population centers and those living in sparsely-populated outlying areas.)

[125] *See* Cahners In-Stat Group, *U.S. Residential DSL Continues to Grow Despite Turmoil*, at 26-27 (Oct. 2001); Eric Knorr, *Mobile Web vs. reality, MIT Technology Review* (June 1, 2001) ("Stray beyond urban areas, furthermore, and it's hard to imagine a nanocell on every fifth fence post."); *see also* Robert E. Hall and William H. Lehr, *Promoting Broadband Investment and Avoiding Monopoly*, at 9 (describing market as a duopoly between an RBOC and a cable provider); *Competitive Analysis of DSL and Cable Modems, Broadband Intelligence,* at 1 (Q3 2001) (same).

just beginning to receive consumer acceptance.[126]

Thus, there plainly could be no across-the-board finding that ILECs lack market power in the provision of retail mass market services. Intermodal competition does not exist in all areas or for all customers, and the ILECs have largely succeeded in snuffing out emerging intramodal competition.[127] These facts alone doom SBC's request for an across-the-board determination of non-dominance.

Instead, a disaggregated analysis of each relevant market is required, "[a]nd the decisive question should be whether, *in a particular arena*, the incumbent LEC has demonstrated that it has neither the ability profitably to raise price by restricting its own output nor the ability to raise price profitably by raising its rivals' costs."[128] Perhaps some ILECs will be able to show that they lack market power with respect to some customers, some services, and some areas – but any such petitions will have to be evaluated on their individual merits.

Moreover, any such petition must confront the basic economic realities, which all

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[126] *See* Cahners In-Stat Group, *U.S. Residential DSL Continues to Grow Despite Turmoil*, at 27 (Oct. 2001); The Yankee Group, *Digital Broadcast Satellite: Market Maturation Underscores New Challenges* 7-8 (Dec. 2001).

[127] *See* RHK Telecommunications Industry Analysis, *Broadband Access: North America, Market Forecast: DSL 2001-2005*, at 1 ("Competition for DSL subscribers in the telecom market is non-existent as more CLECs and DLECs become insolvent."); *id.* at 20 ("RHK expects that the RBOCs will continue to dominate DSL service deployments throughout the forecast period, as there will be little to no competition from financially strapped CLECs and DLECs"); *Wall Street Has More Bad News For CLECs*, *Communications Daily* (Feb. 22, 2001) 2001 WL 5052608 ("Capital markets are 'basically closed' to CLECs" and analysts "predict[] that telecom IPOs would be 'limited or nonexistent in 2001.'"); Cahners In-Stat Group, *U.S. Residential DSL Continues to Grow Despite Turmoil*, at 1 (Oct. 2001) (Because of bankruptcies of start-up DSL providers, the ILECs "are holding the dominant position in the market.").

[128] Willig Decl. ¶ 36 (citing *Notice* ¶ 28) (emphasis added).

point to a very real danger of market power abuse.[129] This analysis should begin with the recognition that ILECs continue to own the wires used to provide virtually all *narrowband* voice and data services. These services are enormously profitable to the ILECs, and the ILECs therefore have strong incentives to take any and all steps to minimize customer alternatives to those services, including broadband. As Professor Willig explains, broadband poses a serious threat to the ILECs' narrowband revenues.[130] Even the ILECs' own DSL services, which the ILECs reluctantly launched in response to emerging cable modem services, draw customers away from their more profitable narrowband access lines.[131] Just recently, the Commission's policy chief recognized this "ripple effect."[132] Customers are canceling second lines, and that is diminishing ILEC profits.[133]

Another reason why ILECs have the incentive to thwart DSL demand and deployment is that, to the extent DSL service is viable, CLECs have a better chance at challenging the ILECs' local *voice* monopolies. As Professor Willig explains, "[g]iven the high cost of using ILEC bottleneck facilities, local entry may not be viable" in the many areas with high network element rates, unless entrants can offer both data *and* voice over a single line.[134]

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[129] *See* Willig Decl. ¶¶ 37, 81-87, 93-113.

[130] *See id.* ¶¶ 81-85.

[131] *See id.* ¶ 85 ("Accordingly, the displacement effect therefore may have a profound impact on the RBOCs' bottom line: *Increasing broadband demand may well reduce RBOC profits.*.").

[132] *Communications Daily*, at 2 (Feb. 21, 2000) (quoting Robert Pepper, chief of Commission Office of Plans and Policy).

[133] *See id.*

[134] Willig Decl. ¶ 87 (emphasis in original); *see also id.* ¶ 14 ("Offering both voice and DSL services over the same ILEC loop may be the best, and perhaps the only, means of profitable competitive entry in many areas.").

As Goldman Sachs put it, "[a] carrier's success will ultimately be determined by its ability to deliver local, long distance, and Internet access over the same pipe."[135] Without the ability to bundle – and the ability to spread the costs of access over multiple services – the CLECs will be unable to compete with the ILECs on the voice front. Indeed, "[a]nything that makes it easier for an ILEC artificially to raise its rivals' costs of providing DSL service over network elements – or, as in the case of an exemption from tariffing requirements, makes it more difficult to detect such anticompetitive actions – may . . . deter local voice entry and competition, at a considerable social welfare cost."[136] Thus, the economic realities create compelling ILEC incentives to constrain the availability of DSL, both through resistance to CLEC and DLEC deployment efforts and through price increases to consumers.

There are, of course, countervailing incentives. For example, where intermodal competition does exist, raising the price of DSL may cause some ILEC customers to switch to cable providers. The question ultimately comes down to which incentive is stronger. Unfortunately for consumers, there is powerful evidence that it is the anti-competitive, anti-broadband ILEC incentive that has prevailed.

Recent events suggest that, not only can ILECs profitably raise the prices of their DSL offerings, but they have in fact done so. After contributing to the collapse of the CLEC and

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[135] Goldman Sachs, Investment Research Report, *The Race to Build the Broadband Kingdom*, at 26 (Aug. 12, 1999).

[136] Willig Decl. ¶ 14; *cf. Deployment of Wireline Services Offering Advanced Telecommunications Capability*, Third Report and Order, 14 FCC Rcd. 20912, ¶ 25 (1999) (explaining that the "lack of access to the high frequency portion of the local loop would materially raise competitive LECs' cost of providing SDSL-based service to residential and small business users, delaying broad facilities-based market entry, and materially limiting the scope and quality of competitors' service offerings.").

DLEC industries, the RBOCs "reverted to their old monopolistic ways."[137] They turned their watches back to "Bell Standard Time,"[138] slowed DSL deployment in areas not served by cable,[139] and then initiated a startling 25% price increase.[140] SBC began the trend by raising the monthly price of its consumer service from $39.95 to $49.95.[141] The other RBOCs soon followed suit.[142] The fact that SBC could initiate such a significant price increase with no concern regarding what others might do confirms the market power it possesses. If SBC were truly non-dominant – if it truly lacked market power – it would, by definition, be a "price taker" and would not find it profitable to initiate such a substantial price hike. Tellingly, while SBC and the other RBOCs were raising DSL prices in this country, DSL prices abroad plummeted.

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[137] RHK, Inc., *Access Network Systems: North America,* p. 1, Dec. 2001; *see also* RHK, Inc., *Broadband Access: North America*, at 1 (Dec. 2001) ("Competition for DSL subscribers in the telecom market is non-existent as more CLECs and DLECs become insolvent.").

[138] Salomon Smith Barney, *Communications Components*, at 2 (Nov. 23, 2001) ("Perhaps most importantly, the fall of the competitive local exchange carriers (CLECs) has given the ILECs room to retire to 'Bell Standard Time' after years of trying to move in sync with 'Internet Time.'").

[139] *See id*. ("The result has been lower than expected DSL rollout rates in the US. In contrast, the worldwide ADSL sky has not fallen. Deployment has gone much more smoothly in several regions such as South Korea, Japan, and most of Europe."); *see also* IDC, *US DSL Market Shares by Vendor, 1H01* (Aug. 2001) ("Now that upstart competitors, such as defunct NorthPoint Communications, no longer threaten the ILECs, the race for DSL subscribers has slowed . . . . The ILECs now dominate the US DSL market, and with a dearth of competition, the ILECs no longer have an incentive to aggressively market and deploy DSL service.").

[140] *See id*.; Teledotcom, *SBC's Coast Is Clear for DSL Rate Hikes* (March 5, 2001), available at http//www.teledotcom.com/article/TEL20010301S0009; *SBC dominates DSL market as others struggle*, *San Francisco Chronicle (*June 13, 2001).

[141] *See id.*

[142] *See id*.; *see also* Willig Decl. ¶¶ 21, 104.

Bell Canada charges only $25.50 (U.S.) for a 1 mbps download connection;[143] prices in Asia fell from $40 to $17 per month during the same period;[144] and British Telecom recently cut its DSL price by *40%*.[145]

The consequences are entirely predictable. Demand for DSL rose sharply in other countries (pulling even with cable in relative shares of subscribers)[146] and did not fare as well in the United States (although, as detailed in Part IV below, DSL growth continued to outpace cable). SBC, for example, suffered a churn rate for DSL of 5.7% *per month* over the first seven months of 2001.[147] In other words, in just over half a year, SBC lost 33% of its existing DSL customers, not to mention the potential customers who *would* have signed up for DSL at $39.95 but were unwilling to do so at $49.95.

SBC's economists Crandall and Sidak claim that this high level of demand elasticity implies that SBC lacks market power.[148] But they ignore a crucial question: What happened to SBC's lost DSL customers? According to the Rappaport study of cross-elasticity, although some of these customers switched to cable, it is likely that *a substantial percentage of*

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[143] *See* Todd Spangler, *Crossing the Broadband Divide*, *PC Magazine*, at 97 (Feb. 12, 2002).

[144] *See* Cahners In-Stat Group, *U.S. Residential DSL Continues to Grow Despite Market Turmoil*, at 25 (Oct. 2001).

[145] *See Communications Daily*, at 6 (Feb. 27, 2002) (reporting that British Telecom announced price reduction from $35 to $21).

[146] *See* Organization for Economic Co-operation and Development, *The Development of Broadband Access in OECD Countries*, at 5, 13 (Oct. 29, 2001) ("*OECD Report*").

[147] *See* Declaration of Robert W. Crandall and J. Gregory Sidak ¶ 68 ("Crandall-Sidak Decl."), submitted in Docket No. 01-337.

[148] *See id.* ¶ 19.

them returned to narrowband dial-up access.[149] And that is precisely what made the price increase profitable for SBC. SBC did not in fact "lose" all of these customers. Many of them simply substituted an additional access line for their broadband service.[150] This is direct and compelling evidence of market power. And it should come as no surprise to SBC, whose own economists cite an econometric study concluding that there is a high elasticity of demand between broadband and narrowband.[151]

It is also confirmation that broadband and narrowband should be considered to be part of the same market for purposes of analyzing market power in this proceeding. Once it is recognized that the two services are within the same relevant market, the inescapable conclusion is that ILECs possess tremendous market power. ILECs provide 94.5% of the lines used to provide narrowband Internet access.[152] Taking into account the ILEC share of DSL lines, ILECs control more than *80%* of the overall lines used to provide Internet access. Moreover, this ILEC dominance is not likely to change dramatically in the near term.[153] Even if broadband subscriptions doubled and there were no gains in dial-up, the ILEC share of customers would still exceed 70%.[154]

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[149] *See* Willig Decl. ¶ 111.

[150] *See id.* at ¶ 112.

[151] *See* Paul Rappaport, Donald J. Kridel, Lester D. Taylor, Kevin Duffy-Deno, *Residential Demand for Access to the Internet*, University of Arizona Working Paper, at 19 (Spring 2001).

[152] *See* FCC, *Federal Communications Commission Releases Latest Data on Local Telephone Competition*, 2, (Feb. 27, 2002).

[153] Willig Decl. ¶ 137.

[154] *See id.*

2. Services Provided at "Wholesale" to Other Carriers (and ISPs). At the wholesale level, there is, if anything, even less of an argument that ILECs lack market power.

(a) Market definition. The geographic market is the same for both wholesale and retail: the boundaries are local.[155] But the product offered in the wholesale market is the *input* necessary to provide retail Internet access service, namely the provision of broadband last-mile transport.

(b) Market power. Even under SBC's market-share-driven analysis, the ILECs clearly have overwhelming market power because they control almost all of the last-mile facilities to which ISPs seeking to provide residential and small business broadband services can turn.[156] That ILECs currently wield market power is true regardless whether the relevant market is deemed to include only "broadband" transport or all local access facilities available to deliver Internet services. In either case, the ILECs own almost all of the necessary inputs. "Virtually all loops terminate in ILEC offices."[157] Thus, if ISPs want to provide retail mass-market broadband services, their only option in most instances is to use the ILECs' facilities.

Adding to the ILECs' dominance is the high elasticity of demand for mass-market broadband services. As SBC notes, the elasticity of demand is "somewhere between –1.2 and –

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[155] *See supra* at 37.

[156] Access to ILEC loops is essential because it permits competitors to provide both broadband data and voice services over a single line, a bundled service that many customers find attractive. *See, e.g.*, Raymond James, *Telecommunications Services Initiation of Coverage, Qwest Communications Intl.*, at 20 (Dec. 10, 2001) ("Qwest estimates that 30% of customers in its 14-state region subscribe to a bundling service").

[157] *See* Fea/Taggart Decl. ¶ 14.

1.45."[158] And as SBC concedes, "[u]nless ISPs are making excess profits when they sell DSL service (which ISPs would presumably deny), they would have to pass on to consumers any price increase by SBC for DSL transport service."[159] Because of the high elasticity of demand, and because ISPs must pass this cost onto the customer, a small artificial cost advantage facilitated through price squeeze will be enough for the ILEC, as it gains § 271 authorization, to price its DSL/ISP bundle at a price at which other ISPs will be unable to compete.

Moreover, there is no indication that the market dynamics are likely to change in the foreseeable future. No one believes that it is generally feasible for CLECs to deploy copper loops to residential customers and thereby provide facilities-based competition. The Commission certainly does not, as evidenced by its *UNE Remand Order*. After developing an extensive factual record, the Commission concluded that CLECs, in general, could not self-provide loops and transport (including high capacity loops and transport used for special access services) or acquire such facilities from third-parties.[160] Likewise, the Commission held that all transport facilities must be unbundled because the factual record demonstrated that the incumbent LECs are generally the only realistic and reliable source of transport, even in large metropolitan areas. Thus, without access to the ILECs' bottleneck inputs, ISPs (and CLECs and DLECs) will likely be eliminated from the mass-market for broadband services.

But there is a more fundamental reason why the Commission must ensure

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[158] SBC Petition at 8; *see also*, Hal R. Varian, *The Demand for Bandwith: Evidence from the INDEX Project*, University of California, Berkeley, at 14-15 (Sept., 2001) ("Users are not willing to pay very much for higher bandwith for accessing today's applications.").

[159] SBC Petition at 24 n.64.

[160] *UNE Remand Order* ¶¶ 176-78, 323-324.

competitive access to the high-frequency portion of the local loop. As explained above, given the high cost of using ILEC bottleneck facilities, local entry may not be viable unless entrants can offer both data *and* voice over a single line.[161] Without the ability to bundle – and the ability to spread the costs of access over multiple services – the CLECs will be unable even to attempt challenge the ILECs' local *voice* monopolies in many areas.

Thus, even if the Commission concludes that the retail mass market is competitive in certain areas of the country for certain consumers, the wholesale mass market is not. The ILECs dominate the wholesale markets, not just in those geographic locations where the retail markets are uncompetitive (although, at a minimum, those locations must necessarily be deemed uncompetitive), but throughout the rest of the country as well. And deregulating these wholesale broadband services would thwart retail competition in both Internet access and voice services.

III. THE ILECS' PERVASIVE MARKET POWER REQUIRES NOT ONLY CONTINUED APPLICATION OF DOMINANT CARRIER REGULATIONS BUT ADDITIONAL, TARGETED INITIATIVES TO DISCOURAGE ILECS FROM RAISING POTENTIAL RIVALS' COSTS.

Because ILECs continue to wield tremendous power in the provision of both large business and mass market broadband services, SBC's request for an across-the-board exemption from dominant carrier regulation of those services must be denied. Indeed, as explained above, it is unlikely that any ILEC could demonstrate the requisite lack of market power with respect to most or all broadband offerings, much less define the exempted offerings in a sufficiently precise way to prevent it from becoming an anticompetitive loophole. The continued application of dominant carrier regulation is thus entirely appropriate, for tariffing and related regulations continue to perform an invaluable and pro-competitive role in the broadband context by

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[161] *See supra* at 45.

providing needed transparency and by reducing transaction costs, all at very little real expense to the ILECs. In fact, in light of the overwhelming evidence of enduring ILEC market power and the clear danger it poses to both broadband and narrowband competition, a strong case can be made that *additional* dominant carrier regulations, such as structural-separation and affiliate-dealing rules, are needed.

Even more importantly, the same market power facts confirm, beyond doubt, that the Commission must resist ILEC efforts in other proceedings to dismantle existing requirements that ILECs provide non-discriminatory access to their bottleneck facilities to competitors seeking to provide competing broadband and narrowband services. Indeed, as the fragile base of potential competitors and competitive activity continues to crumble, it has become increasingly clear that more is needed to shore up these regulations. As detailed below, there are a number of targeted, pro-competitive steps that the Commission can and should take in other proceedings that not only will not slow, but will encourage, broadband deployment and competition.

A. The Commission Must Maintain Existing Dominant Carrier Regulations.

As the Supreme Court has stated, "[t]he tariff-filing requirement is . . . the heart of the common-carrier section of the Communications Act."[162] Where market power is absent, competitive forces generally ensure enforcement of the central common carrier goal of just, reasonable and nondiscriminatory rates. Where market power exists, however, tariffing and related regulation must bridge the gap. Without the transparency provided by the tariffing

[162] *MCI Telecoms* v. *AT&T*, 512 U.S. 218, 229 (1994).

requirement, "[t]he provisions allowing customers and competitors to challenge rates as unreasonable or as discriminatory would not be susceptible of effective enforcement."[163]

For that reason, dominant carriers are required to file tariffs that disclose not only the carriers' rates (and other terms and conditions of service),[164] but also supporting data,[165] including when rates are changed, and supporting "economic information."[166] By providing notice (ranging from a minimum of one day's notice for new services of price cap LECs to fifteen days' notice for rate increases to existing services),[167] a tariff "allows both the FCC and affected customers to review and challenge price changes by LECs."[168] When the Commission determines that a tariff does not sufficiently show that the rates and charges contained therein are "just and reasonable," the Commission may reject the tariff and order refunds.[169] Perhaps most critically, however, the tariff requirement may deter some market power abuses in the first

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[163] *Id*. at 230; *see also AT&T* v. *Central Office Tel*., 524 U.S. 214, 222 (1998) (concluding that tariffs are required in order to "prevent[ ] unreasonable and discriminatory charges").

[164] 47 U.S.C. § 203(a); 47 C.F.R. § 61.31; *see also* 47 C.F.R. § 61.19(c) ("No carrier required to file tariffs may provide any interstate or foreign service communication until every tariff publication for such communication service is on file with the Commission and in effect").

[165] *See generally* 47 C.F.R. § 61.38.

[166] *Id*.

[167] *See* 47 C.F.R. § 61.58.

[168] *WorldCom, Inc.* v. *FCC*, 238 F.3d 449, 454 (D.C. Cir. 2001).

[169] *See, e.g.*, *Southwestern Bell Tel. Co.* v. *FCC*, 138 F.3d 746, 752 (8th Cir. 1998) (affirming Commission decision to reject LEC tariffs that failed to justify their costs). At the same time, the Commission has acted to reduce the costs of tariffing by, for example, permitting electronic filing. *See, e.g., 1998 Biennial Regulatory Review – Part 61 of the Commission's Rules & Related Tariffing Requirements*, Report and Order and First Order on Reconsideration, 14 FCC Rcd. 12293, ¶¶ 5-6 (1999). Thus, tariffing is an increasingly efficient way for the Commission to ensure that it, and all interested parties, can test the reasonableness of dominant firms' rates and charges.

instance, because the transparency that tariffing provides makes it more likely that misconduct will be detected and punished.[170]

Tariffing and related dominant carrier regulations are no less important with respect to broadband services than they are with respect to traditional narrowband services. As the Commission has concluded, "incumbent LECs . . . have the incentive and ability to discriminate against competitors in the provision of advanced services."[171] This incentive, which is generally a product of "their monopoly control over key inputs that rivals need in order to offer retail services," "exists in all retail markets in which they participate."[172]

The Commission has recognized that the risk of discrimination is particularly acute in the advanced services market. For one thing, regulators cannot easily detect "[d]iscrimination against competitors wishing to innovate and deploy technology different from that deployed by the incumbent LEC."[173] As new technologies emerge, both consumers and the Commission will need detailed information in order to determine that discrimination is not occurring.[174] And broadband-related discrimination "likely will cause a significant setback to

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[170] Currently, the Commission's maximum penalties are not adequately severe, and the ILECs view them as a mere cost of doing business. AT&T addresses this issue is more depth in other ongoing proceedings. *See Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321 (Jan. 22, 2002); *Performance Measurements and Standards for Unbundled Network Elements and Interconnection,* CC Docket No. 01-318 (Jan. 22, 2002).

[171] *SBC-Ameritech Merger Order* ¶ 186.

[172] *Id*. ¶ 190.

[173] *Id*. ¶ 205.

[174] On at least one occasion, for example, DSL tariffing has permitted the Commission to determine that RBOC claims that line sharing was "technically [in]feasible" likely were untrue. *Deployment of Wireline Servs. Offering Adv. Telecoms. Capability*, First Report and Order and Further Notice of Proposed Rulemaking 14 FCC Rcd. 4761, ¶ 103 (1999).

current and future efforts to encourage competition and innovation in the provision of new types of advanced services."[175] As the Commission has noted, "[i]ncumbent LEC discrimination against competitive providers of xDSL services has delayed competitive provision of these services and necessitated regulatory intervention."[176] As detailed above, ILEC discrimination is no mere theoretical concern, but a well-documented matter of immediate concern with respect to both large business and mass market broadband services.

The benefits of the increased transparency and efficiencies provided by dominant carrier regulation are perhaps most obvious with respect to the DSL-based telecommunications services that ILECs sell to ISPs. Absent tariffing, ILEC discrimination (price and non-price) against ISPs would be easy to accomplish, difficult to detect, and, particularly as ILECs gain interLATA authority, increasingly prevalent.[177] Indeed, the only reason why ILECs provide transport service to ISPs is because they are required to do so under the Commission's *Computer* rules (which the ILECs also seek to dismantle in the name of "broadband" deployment).[178] The transparency that tariffing provides plays a vitally important role in reducing the risks of discrimination and price squeezes that would impede ISP competition. Tariffing, together with the *Computer* rules, also helps prevent ILECs from unilaterally raising ISP rivals' transaction

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[175] *SBC-Ameritech Merger Order* ¶ 187.

[176] *Id.* ¶ 197.

[177] *See, e.g.*, T. Brennan, *Why Regulated Firms Should Be Kept Out of Unregulated Markets: Understanding the Divestiture in* United States v. AT&T, 32 Antitrust Bulletin 741, 754 (1987) ("If [Verizon] can provide its products to others at higher rates than it charges itself, or at lower quality, then it creates a similar margin that it can exploit by raising prices in the downstream market").

[178] *See Computer III Further Remand Proceedings: Bell Operating Co. Provision of Enhanced Servs.*, Report and Order, 14 FCC Rcd. 4289, ¶ 13 (1999).

costs (and delaying entry) by drawing out the negotiation process. With tariffing, all an ISP need do is to follow the procedures for ordering the tariffed DSL transport service.

Tariffing is equally important in the context of end user bundles of DSL and ISP services, particularly to ensure that ILECs are not using such bundles in an anticompetitive fashion (*e.g.*, to facilitate cross-subsidization) and that BOCs do not violate § 271 of the Act by providing the ISP service that the Commission has determined is an interstate service. As the Commission has acknowledged, the premature provision by RBOCs of interLATA services would give them "an enormous benefit in strengthening their position in the telecommunications marketplace," "afford them a significant 'jumpstart' when they do obtain Section 271 authorization," and "strengthen and entrench their relationships with their in-region local customers."[179] And the tariffing of ILEC DSL (and other "advanced" services) greatly simplifies the detection (and hence the deterrence) of such illegal and anticompetitive conduct.

As the Commission recognized just four years ago, federal tariffing of advanced services has enabled the Commission "successfully [to] forestall[] attempts by incumbent LECs to shift costs to monopoly services in order to justify rates that effect a price squeeze."[180] That is no less true today, and thus the Commission should maintain the current requirement that ILECs tariff their advanced services offerings and the inputs sold to competitors.

The current inquiry also supports continuing dominant carrier rate regulation (which, for the large ILECs, exists today as price cap regulation). There is no basis for creating

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[179] *AT&T Corp.* v. *Ameritech Corp. & Qwest Communications Corp.*, Memorandum Opinion and Order, File No. E-98-41, 1998 WL 996054, ¶¶ 40-42 (1998).

[180] *GTE Tel. Operating Cos.*, Memorandum Opinion and Order, 13 FCC Rcd. 22466, ¶ 32 (1998); *see also Bell Atlantic Tel. Cos.*, Memorandum Opinion and Order, 1998 WL 823494, ¶ 14 (1998).

an exception for advanced services over which the ILECs retain market power. To the contrary, as noted above, recent experience with ILECs that have been granted "Phase II" pricing flexibility for "broadband" transport and special access services, starkly confirms the continuing need for rate regulation. The ILECs that have received such flexibility have not reduced their rates, as the Commission had hoped, but have opportunistically *increased* their rates.[181]

In fact, given the marketplace realities and the ILECs' recent track record, a strong case can be made that the Commission should strengthen, not weaken, dominant carrier regulations. For example, if ILECs are to be allowed to provide ISP services and retail data services while they continue to control bottleneck facilities, the Commission should apply structural separation and separate affiliate rules. Properly executed structural separation helps ensure that separate affiliates are *functionally* separate, so that regulators, as well as competitors, can identify "the rates, terms, and conditions on which services will be available to all potential purchasers."[182] Such separate corporate affiliates would, for example, maintain separate books, records, and accounts from the "wholesale" arm, maintain separate facilities, and deal at arms length, in writing, with the wholesale arm. Structural separation "is a pragmatic and moderate attempt to enable dominant producers or suppliers whose participation in a given market raises special problems to participate, while reducing the risks that their customers or competitors will be disadvantaged by such participation."[183] In the area of telecommunications, "there is nothing

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[181] *See* Comments of AT&T, *MAG Plan for Regulation of Services of Non-Price Cap Incumbent Local Exchange Carriers*, CC Docket No. 00-256, at 19-22 (Feb. 14, 2002).

[182] *Amendment of Section 64.702 of the Commission's Rules and Regulations (Second Computer Inquiry), Final Decision and Order*, 77 FCC 2d 384, ¶ 205 (1980) ("*Computer II*").

[183] *Id.* ¶ 205.

novel about . . . separate subsidiary requirements."[184] This Commission has found structural separation requirements to be useful for preventing cross-subsidization and protecting against monopoly power abuses in a number of contexts,[185] and it would clearly foster competition in this context.

Structural separation of the ILECs' retail broadband arms from their wholesale divisions would be a "most effective tool" in breaking the ILECs' "resistance to market-opening regulations."[186] Currently, an ILEC has the incentive to charge competitors the highest rates it can for transport, because, no matter what it charges others, it pays only the actual economic cost of using its network.[187] However, if an ILEC's retail broadband business were structurally separate from its network business, for example, the retail business would have to pay the same

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[184] *GTE Midwest* v. *FCC* 233 F.3d 341, 345 (6th Cir. 2000).

[185] *See, e.g., id*. at 348 (affirming FCC rules requiring structural separation of LECs' landline and commercial mobile radio services); *Illinois Bell Tel. Co.* v. *FCC*, 740 F.2d 465, 472 (7th Cir. 1984) (affirming FCC regulation requiring structural separation of BOCs' consumer premises equipment services); *Computer and Communications Indus. Assn.* v. *FCC*, 693 F.2d 198, 218-19 (D.C. Cir. 1982) (affirming *Computer II*, structural separation requirements as to advanced services); *GTE Servs. Corp.* v. *FCC*, 474 F.2d 724, 732 (2d Cir. 1973) (affirming the structural separation requirements as to data processing services in *Regulatory and Policy Problems Presented by the Interdependence of Computer and Communications Services and Facilities*, Final Decision and Order, 28 FCC 2d 267 (1971)); *Application of GTE Corp., Transferor, and Bell Atlantic, Transferee*, Memorandum Opinion and Order, 15 FCC Rcd. 14032 ¶¶ 260-73 (2000) (requiring structural separation of advanced services affiliates) ("*Bell Atlantic-GTE Merger Order*"); *SBC-Ameritech Merger Order* ¶¶ 363-70 (same).

[186] *Congress Should Consider Structural Separation of Bells*, Communications Daily, at 8 (Feb. 22, 2002) (quoting Professors Robert E. Hall and William H. Lehr); *see also id*. (reporting that structural separation would remove any "incentive to hobble the operations of new" CLECs and DSL providers); Robert E. Hall and William H. Lehr, *Promoting Broadband Investment and Avoiding Monopoly*, at 13 (Feb. 21, 2002).

[187] *See, e.g., Bell Atlantic-GTE Merger Order* ¶ 166 ("[T]he incumbent LEC may profit from imposing high loop charges, or access charges, on both its affiliates and its competitors, because the charges to its affiliates constitute only an internal transfer").

price for transport as do competitive ISPs. Because structural separation includes the mandate that the retail arm of an ILEC not be permitted to sell services below its costs,[188] an ILEC would, for the first time, have at least some incentive to moderate rates for bottleneck facilities so that its retail arm could effectively compete.[189]

B. The Commission Must Shore Up Its Regulations Implementing The ILECs' Obligations To Provide Non-Discriminatory Access To Their Bottleneck Facilities.

Although, as explained above, it is clear that tariffing and related dominant carrier regulation place some important checks on anticompetitive ILEC broadband conduct, it strains credulity to believe that it was those dominant carrier regulations that motivated the SBC Petition and the massive lobbying effort associated with it. Rather, SBC and its brethren hope to catch the Commission off guard in this proceeding and parlay superficial market power analysis to their advantage in the far more important proceedings in which the Commission is examining the ILECs' systematic efforts to preclude most retail broadband (and narrowband) competition altogether by denying competitors access to the facilities necessary to provide those retail

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[188] This imputation would not impede universal service support. The retail arm would not be allowed to price service below cost, but the "price" would include any support the retail arm receives from a universal service fund or, until such time as an appropriate universal service fund is established, from whatever other mechanisms the Commission has in place to support affordable basic service in high cost areas. To comply with the 1996 Act, of course, such support must be nondiscriminatory. *See* 47 U.S.C. § 254.

[189] SBC's argument that the Commission should forbear from applying tariff requirements to SBC's provision of advanced services," SBC Petition at 73, must also be rejected. SBC argues that lack of market power is the touchstone for forbearance under 47 U.S.C. § 160, which governs the Commission's authority to forbear from applying specific regulations or statutory provisions. And, as demonstrated above, ILECs do, in fact, exercise significant "market power" in myriad ways with respect to their provision of "broadband" services and therefore the criteria set forth in § 160(a) cannot be met. And, even if an absence of "market power" in some specific geographic areas were sufficient to justify forbearance in some instances, § 160(a) makes clear that such a determination can be limited to "some of [a carrier's] . . . geographic areas." *Id.*

services.

The ILECs have asked the Commission to "de-UNE-fy" high capacity transmission facilities, even though the reality is that CLECs are critically dependent upon ILEC loop and transport facilities in providing local telecommunications services, including high-speed data services to businesses.[190] The ILECs have also sought to deny CLECs access to critical last mile loops in cases where they have deployed NGDLC.[191] And, rounding out their anti-competitive wish list, ILECs have demanded that the Commission: (1) relieve them of all line sharing and line splitting obligations;[192] (2) forbid competitive LECs that pay for entire "loops" from offering data services over those loops;[193] (3) dismantle broadband-related collocation obligations; (4) lift the § 254(c)(4) resale requirement with respect to broadband

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[190] Opposition of AT&T to Joint Petition, *Implementation of the Local Competition Provisions in the Local Telecommunications Act of 1996*, CC Docket No. 96-98, at 18-29 (June 11, 2001). Indeed, the only thing that has changed since the Commission found that CLECs would be impaired without access to ILEC high capacity transmission facilities, *see UNE Remand Order* ¶¶ 176-78, 323-324, is that the financial markets have closed to CLECs and CLECs have even less ability to self-deploy these bottleneck facilities. AT&T will address this issue in detail in its Triennial Review Comments.

[191] The ILECs have argued that, when they deploy NGDLC in their loop plant, the NGDLC is not part of the loop but rather "packet switching." *See, e.g.*, Comments of SBC, *Deployment of Wireline Services Offering Advanced Telecommunications Capability*, CC Docket No. 98-147 (Feb. 27, 2001); Reply Comments of Verizon, *Deployment of Wireline Services Offering Advanced Telecommunications Capability*, CC Docket No. 98-147 (March 13, 2001). Thus, according to the ILECs, CLECs can gain access only to the copper portion of the loop – a point of access that is both technically and economically infeasible.

[192] *See* Comments of SBC/BellSouth, *Inquiry Concerning High-Speed Access to the Internet Over Cable and Other Facilities,* GN Docket No. 00-185, at 19-23 (Dec. 1, 2000); Comments of Verizon, *Inquiry Concerning High-Speed Access to the Internet Over Cable and Other Facilities,* GN Docket No. 00-185, at 27-28 (Dec. 1, 2000).

[193] *See* Comments of SBC/BellSouth, *Inquiry Concerning High-Speed Access to the Internet Over Cable and Other Facilities,* GN Docket No. 00-185, at 20 n.55 (Dec. 1, 2000).

services; and, for good measure, (5) forbear from applying the requirements of § 271 to advanced services.[194] It is no exaggeration that granting these ILEC requests would put an end to most DSL competition (and the few remaining DLECs), and, by denying CLECs revenue streams and customers (*i.e.*, customers that value single line voice and DSL service) that are available to the ILECs, put an end to much voice competition as well (and hence the few remaining CLECs). The Commission should firmly reject each of these anti-competitive requests.

Moreover, it is now clear that more must be done to ensure that competitors have nondiscriminatory access to the facilities they need to compete. At a minimum, the Commission should take the following pro-competitive actions:

Reform Necessary to Facilitate Deployment of CLEC Facilities. The Commission should eliminate existing barriers that preclude CLECs from deploying facilities necessary for effective voice and broadband competition. Most critically, the Commission should eradicate the current use restrictions that deny CLECs access to loop-transport combinations (called "EELs") that are critical to CLECs' ability to deploy their own network facilities.[195] Access to EELs will make it possible for CLECs to aggregate traffic over broader geographic regions and thereby make it economic for CLECs to deploy switches and transmission facilities.[196] Because they

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[194] *See id.* at 19-23.

[195] *See generally* Comments of AT&T, *Implementation of the Local Competition Provisions in the Local Telecommunications Act of 1996*, CC Docket No. 96-98 (April 5, 2001) ("*AT&T Use Restriction Comments*").

[196] *See UNE Remand Order* ¶ 288 (EELs allow CLECs "to aggregate loops at fewer collocation locations and increase their efficiencies by transporting aggregated loops over efficient-high capacity facilities to their central switching location").

have small customer bases relative to the ILECs, CLECs can economically deploy high capacity fiber transport facilities in only limited circumstances. But in order to provide high capacity services broadly, CLECs must still be able to reach those customers located in regions where the CLECs cannot justify self-supplying fiber. By purchasing EELs, a CLEC can "fill in" its network in areas where the CLEC simply does not have sufficient traffic to justify a facilities build. A CLEC can purchase UNEs to transport traffic from LSOs where it has relatively low demand to a central hub where that demand is aggregated using a multiplexer. Then the CLEC can deploy its own fiber transport facilities to connect the various hubs. In this way, the CLEC ensures that the fiber it deploys is utilized as fully as ILEC fiber transport and the CLEC can reach all the customers that the ILEC can reach. Recognizing the value of EELs to CLECs, the ILECs have continued to impose use restrictions. Without an effective response from the Commission, the ILECs will succeed in limiting the geographic areas in which CLECs can deploy transmission and switch facilities, and will thus prevail in thwarting facilities-based competition.

In addition, the Commission must prevent ILECs from abusing the "hot cut" process, if CLECs are ever to be able to provide facilities-based broadband services to residential customers. For mass-market customers, it is simply not economic for CLECs to replicate existing ILEC loop facilities, but many CLECs have attempted to compete on a facilities basis by collocating their transport facilities at ILEC LSOs and leasing ILEC-provided loops. These efforts, unfortunately, have failed. The problem is that the CLECs depend upon the ILECs for "hot cuts," whereby the customer's loop is manually disconnected from the ILEC network and transferred to the CLEC network. It is well-documented that the hot cut process represents a major hurdle to competition, not only because of the expense associated with the process and the

significant risk of outages to the customer, but also because of the ILECs' refusal to perform hot cuts properly or in volumes sufficient to support broad-based competition.[197] Customers often are unwilling to risk the service interruptions that frequently arise out of the hot cut process, and thus are unwilling to switch to a CLEC's service.

The use of manual hot cuts is driven by the existing network architecture that ILECs have employed. As AT&T will explain in the Triennial Review Proceeding, recent technological advances could permit hot cuts to be accomplished electronically, thereby avoiding service interruption. But until the hot cut problem is solved and CLECs have the ability to compete on an equal footing with ILECs, the Commission should ensure that ILECs perform "hot cuts" effectively and efficiently.

Reform Necessary to Discourage ILEC Discrimination. Of course, it is simply not feasible for CLECs to replicate entirely the ILECs' ubiquitous network of over 14,000 central offices and over 220 million loops.[198] Thus, in order to provide both voice and data services to business, it is necessary for CLECs to lease access to ILEC facilities at cost-based rates and upon non-discriminatory terms and conditions. Predictably, the ILECs have sought to abuse their control over bottleneck facilities by providing "access" that does not allow CLECs to use UNEs in a commercially reasonable manner.[199]

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[197] *See, e.g., id.* ¶¶ 265-66, 271.

[198] *See* Federal-State Joint Board, *Universal Service Monitoring Report*, Tables 10.1, 10.2 (Oct. 2001).

[199] *See* Comments of AT&T, *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 1-6 (Jan. 22, 2002); Comments of AT&T *Performance Measurements and Standards for Unbundled Network Elements and Interconnection*, CC Docket No. 01-318, at 2-4, 6-10 (Jan. 22, 2002).

As AT&T has explained in the *Performance Measurements and Standards* proceedings, this dire situation will change only if the ILECs are subject to detailed metrics that make transparent the speed and quality upon which an ILEC provisions network facilities (both network elements and special access) to itself relative to competitors.[200] The Commission must also strengthen enforcement mechanisms in order to ensure that ILECs comply fully with their obligations to provide UNEs on a timely and reasonable basis.[201] Existing penalties are simply insufficient to outweigh the advantages the ILECs gain from providing CLECs patently inferior access to their networks.

The Commission should also confirm that CLECs have access to the entire, or "unified," loop regardless of the architecture used.[202] ILECs have denied CLECs the type of access that allows them to use the full functionality of the loop when the ILECs use NGDLC. Nothing about the "next generation" loop architecture changes any of the fundamental legal principles that have guided the Commission's definition of the local loop over the years. In particular, the local loop has always been defined by its functionality and is not limited to particular services or technologies. Thus, the Commission should confirm that ILECs are providing a requesting carrier with unbundled access to the entire loop network element,

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[200] *See* Comments of AT&T, *Performance Measurements and Standards for Interstate Special Access Services*, CC Docket No. 01-321, at 23-35 (Jan. 22, 2002).

[201] *See id*. at 36-43; *see also* Comments of AT&T, *Performance Measurements and Standards for Unbundled Network Elements and Interconnection*, CC Docket No. 01-318, at 23-38 (Jan. 22, 2002).

[202] A full description of AT&T's position on this issue is found in its October 12, 2000 and February 27, 2001 Comments, and November 27, 2000 and March 13, 2001 Reply Comments in CC Docket Nos. 98-147 and 96-98, hereby incorporated by reference.

regardless of the loop architecture deployed by the ILEC. If CLECs are denied access to a single "unified" loop network element when ILECs deploy next generation network facilities – as the ILECs are now seeking to do – CLECs will be effectively foreclosed from offering broadband services to customers served by those facilities.[203]

Reform Necessary to Protect Competition for InterLATA Data Services. In its *Pricing Flexibility Order*, the Commission gutted the regulations that constrained the prices ILECs could charge for special access services. The Commission's intent was a laudable one – allow ILECs to *lower* rates in response to competition. The reality, however, has not measured up to expectations. As shown above, instead of reducing rates, ILECs have actually *raised* rates.[204] Urgent reform of the Commission's special access regulation is therefore needed. The combination of increased BOC entry into long distance markets and the ability to charge supra-competitive special access rates will give BOCs the unrestrained ability to dominate interLATA data (and voice) services. Long-distance carriers will simply not be able to compete if they are charged monopoly rates for special access services while ILECs obtain this same access at cost.

IV. DEREGULATION OF ILEC BROADBAND SERVICES CANNOT BE JUSTIFIED UNDER AN APPROACH THAT IGNORES MARKET POWER IN PURSUIT OF INCREASED BROADBAND DEPLOYMENT OR "REGULATORY PARITY."

For the most part, SBC acknowledges that this proceeding must focus on market

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[203] *See generally* Comments of AT&T, *Wireline Services Offering Advanced Telecommunications Capability*, CC Docket No. 98-147 (Feb. 27, 2001, Oct. 12, 2000); Reply Comments of AT&T, *Wireline Services Offering Advanced Telecommunications Capability*, CC Docket No. 98-147 (March 13, 2001, Nov. 27, 2000).

[204] *See supra* at 46-47.

power.[205] But perhaps recognizing that it cannot prevail if the Commission's inquiry remains faithful to this traditional market power focus, SBC suggests that the Commission also be guided by more general goals of rapid and reasonable broadband deployment.

AT&T embraces the goal of rapid and reasonable broadband deployment. In fact, in its comments to the National Telecommunications and Information Administration, AT&T proposed and defended a four-part plan for achieving that goal,[206] including the elimination of *unnecessary* regulation.[207] When markets are fully competitive and the participants in question cannot exercise market power in the ways described above – the Commission plainly should rely on market forces instead of government intervention. That way, "Americans [will] receive the benefits that robust competition can bring to broadband deployment – lower prices, more choices, technological innovation, and increased productivity."[208] Where, as here, pervasive ILEC market power exists, however, "there remains a continuing need for effective government oversight and enforcement" to protect consumers from monopolists.[209]

SBC's proposed approach of deregulating ILECs without regard to the impact on competition and consumers would benefit no one but the ILECs. This approach could encourage broadband deployment – if at all – only at the unacceptable and unlawful cost of reducing broadband and voice *competition*.

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[205] *See* SBC Petition at 11.

[206] *See* Comments of AT&T, *Request for Comments Deployment of Broadband Networks and Advanced Telecommunications*, Docket No. 011109273-1273-01 (National Telecommunications and Information Administration, Department of Commerce) (Dec. 19, 2001).

[207] *See id*. at iii-iv, 5-7.

[208] *Id*. at 7.

[209] *Id*. at 5.

In any event, SBC has not come close to showing that any of the regulations it seeks to eliminate has posed any impediment to the reasonable rollout of broadband services. As the Commission recently found, "advanced telecommunications is being deployed to all Americans *in a reasonable and timely manner*."[210] What is more, "the availability of and subscribership to advanced telecommunications has increased significantly," "investment in infrastructure for advanced telecommunications remains strong," and "technological and industry trends . . . indicate that alternative and developing technologies will continue to be made available to consumers."[211]

SBC nonetheless makes two unsubstantiated claims. First, it asserts – without any supporting data and despite public statements to the contrary – that the costs of the regulations it seeks to remove have slowed its provision of broadband services.[212] Second, SBC claims that abandonment of such regulations is necessary to establish "regulatory []parity" with its cable company rivals.[213] Even setting aside that many of the services at issue here are not even provided by cable companies (*e.g.*, large-business services, small-business services, and DSL transport), SBC's argument misrepresents both the facts and the law.

A. Compliance With Non-Dominant Carrier Regulation Has Not Discouraged Broadband Investment.

In its Petition, SBC makes no effort to show that the relatively minor costs

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[210] *Third Section 706 Report* ¶ 1 (emphasis added).

[211] *Id.*

[212] *See* SBC Petition at 3 ("[Absent regulatory change], SBC and other incumbent LECs will lack incentives to invest aggressively in broadband infrastructure or new broadband services. Thus, how the Commission decides this issue, and how quickly, will dramatically influence broadband investment and deployment decisions by SBC and other incumbent LECs.").

[213] *Id.* at 5-7.

associated with its tariffing and related regulatory obligations have even a marginal impact on its investment plans with respect to the deployment of its broadband services. That omission is not an oversight because no ILEC could show that the costs associated with tariffing have any real effect on its decisions to upgrade facilities and provide new services. Indeed, ILECs continue to inform their investors of the billions of dollars in upgrades that they have implemented, all the while subject to the regulatory regime that they now seek to dismantle. It is simply inconceivable that an ILEC would decide whether or not to make such investments based upon the nominal burdens associated with tariff filing – which can now be accomplished electronically. Rather, these dominant carrier regulations impose costs that are truly *de minimis*.[214] In short, there is simply no reliable evidence that retail regulations have deterred DSL investments.[215]

Rather, as the Commission has explained, "investment in infrastructure for

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[214] SBC's curtailing of its "Project Pronto" and initiation of passive-optical-network ("PON") trials serve as an example of what motivates ILEC broadband decisions. SBC's chief technical officer explained that it was the cost of active electronics that contributed to Project Pronto's demise. *See Alcatel Rolls Out PON in Western Cable Show Debut, Electronic Engineering Times* (Dec. 3, 2001). Because PONs require no amplifiers or fiber nodes that often demand high maintenance, costs are lower. These reduced costs "was a motivation for SBC Communications Inc. to begin PON trials in California." *Id.*; *see also PONs: Ready, Set, Go!, Telecommunications* (Sept. 1, 2001) (reporting that PONs require less maintenance and that Bell South and SBC have recently ramped PON initiatives).

[215] Nor have the unbundling and other regulations that the ILECs oppose in other proceedings deterred investment, as AT&T will explain in those other proceedings. For example, ILECs complain about unbundling rules, pursuant to which competitors pay TELRIC-based rates that the Commission has found reflect competitive market levels and allow for "normal" profits. *See Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, First Report and Order, 11 FCC Rcd 15499, ¶¶ 679-80 (1996) (concluding that TELRIC-based prices allow for "normal" profits, which are the profits recovered in a competitive market). Normal profits do not deter investment, and it is therefore clear that what the ILECs want is the ability to charge non-competitive rates and obtain "supra-normal" profits. *Id.* ¶ 679.

advanced services remains strong" and "[a]nalysts differ . . . as to which technology will ultimately take the lead."[216] These conclusions are unassailable. In recent years the ILECs have made extraordinary investments in broadband facilities and services in response to competition,[217] and today they provide more than 90% of residential DSL services. Verizon currently can provide high-speed service to more than three-quarters of its access lines,[218] and BellSouth plans to be capable of delivering advanced services to 76% of its customers by year-end.[219] Indeed, supply for broadband services has exceeded even the growing demand,[220] as some price-sensitive consumers prefer to stick with narrowband services.[221] To be sure, investment recently has slowed somewhat, but this trend has been "caused by the economic downturn generally and, more particularly, over-building by carriers, over-manufacturing by vendors, and over-capitalization by financial markets, coupled with unrealistic market

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[216] *Third Section 706 Report* ¶ 1, 68*; see also* James K. Glassman, *Tauzin-Dingell: Network to Nowhere* (Feb. 7, 2002) ("Growing at better than an 80 percent clip, broadband is alive and well in the United States").

[217] *See Third Section 706 Report* ¶ 69 (noting that "[i]n 2000, [ILECs] invested almost $29.4 billion in infrastructure," a "substantial portion" of which investment is "in high speed or advanced data services").

[218] *See* News Release, Verizon, *Verizon Communications Reports Solid Results for Fourth Quarter, Provides Outlook for 2002* (Jan. 31, 2002).

[219] *See* News Release, BellSouth, *Bell South Captures 620,500 DSL Customers and Deploys Broadband Capabilities to More Than 15.5 Million Lines* (Jan 3, 2002).

[220] *See Third Section 706 Report* ¶ 106 (noting "excess capacity").

[221] *See* Comments of AT&T, *Request for Comments Deployment of Broadband Networks and Advanced Telecommunications*, Docket No. 011109273-1273-01 (Dec. 19, 2001). A Strategis Group survey, as reported by ITAA, found that just over one-third of online consumers would be willing to pay $25 per month for the service, but only 12% would be willing to pay $40 or more per month. ITAA, *Building a Positive Competitive Broadband Agenda*, at 10; *see also* SBC Petition at 8, 44-47 (describing high price elasticity of demand).

expectations by investors."[222] Not even monopolists are entirely immune from the effects of an economic downturn.

Nor is dominant carrier regulation in any way preventing the ILECs from competing for customers. ILECs' DSL services have experienced acceptance and growth rates that rival the most successful consumer products of all time. DSL, to be sure, got a late start, on account of the ILECs' attempts to protect their existing second line, T-1, and ISDN services.[223] Not until they fell behind their cable competitors did the ILECs remove DSL from the shelves of inactivity. But in the few short years since the ILECs have begun competing in earnest using their ubiquitous networks and marketing channels, the ILECs have plainly put to rest any concerns that DSL is competitively disadvantaged or that the current regulatory regime is impeding growth.

As one analyst recently noted: "The proliferation of DSL in the telecom industry has seen one of the fastest technology adoption rates ever recorded."[224] Whereas there were only

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[222] *See Third Section 706 Report* ¶ 62 (citing *U.S. Communications Infrastructure at a Crossroads: Opportunities Amid the Gloom*, McKinsey & Company, Goldman, Sachs & Co., at 1, 5-7, 11, 37-40 (Aug. 2001); TeleChoice Sees Slower But Still Substantial Growth in DSL Market (visited Feb. 5, 2002) <www.xdsl.com/content/tcarticles/wp081101.asp>; *Yankee Group Forecasts 2002 DSL Revenues at Over $3.3 Billion*, Yankee Group New Releases (Jan. 11, 2002)).

[223] *See id*. at 2; Cable Services Bureau, *Broadband Today*, Report No. CS 99-14, at 27 (Oct. 1999) ("Although the ILECs have possessed DSL technology since the 1980s, they did not offer the services, for concern that it would negatively impact their other lines of business."); Richard Bilotti, Morgan Stanley, *Telecom – Cable: Residential Broadband Update* (Oct. 15, 2001) ("While DSL technology has been available for many years, it was never offered to customers for fear it would cannibalize existing revenue streams for the RBOCs."); Reinhardt Krause, *Regional Bells Feel Hemmed in – They've Fought Off Upstart, but Cannibalize Themselves with New Services, Investors Business Daily* (Nov. 19, 2001).

[224] *DSL Market: Demand Doesn't Seem To Be An Issue, But Carrier Deployment Execution Does*, Robertson Stephens (January 3, 2001).

50,000 DSL subscribers in the U.S. in 1998, there were over 3.5 million by the end of 2001.[225] The number of U.S. DSL subscribers has grown over 7000% in the last three years.[226] And the growth continues, as DSL posted record gains in the fourth quarter of 2001,[227] despite the ongoing recession and SBC's decision to initiate a 25% price hike.[228] Beyond any doubt, "[t]here have been tremendous recent increases in availability of DSL due to investments in deployment."[229]

The ILECs have been raving about their success to everyone except policymakers in Washington. In its fourth quarter announcements, Verizon reported that its DSL subscriptions increased *122%* in 2001, that the company expected another 50-75% increase in 2002, and that it

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[225] *See* Morgan Stanley, *Residential Broadband Update*, at 33 (Dec. 28 2001); *see also* Press Release, FCC, *Federal Communications Commission Releases Data on High-Speed Services for Internet Access*, at 2 (Aug. 9, 2001) (noting that the number of DSL lines grew 435% to 2 million lines in 2000); *Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996*, Third Notice of Inquiry, CC Docket No. 98-146, ¶ 16 (Aug. 10, 2001) ("[T]he number of ADSL subscribers is growing faster than the number of cable subscribers."); *id*. ¶ 20 ("[T]he data also show continued rapid growth by all technologies, with ASDL gaining significantly on cable's lead.").

[226] *See* Morgan Stanley, *Residential Broadband Update* 33 (Dec. 28 2001).

[227] *DSL Posts Record Gains During Q4, Broadband Daily* (Feb. 4, 2002); *see also* Communications Daily (Feb. 13, 2002) (reporting that "U.S. DSL lines totaled 4.4 million at end of year, up 542,000 [or 14%] from end of 3rd quarter")

[228] *See* Willig Decl. ¶ 108, 145 (explaining that the DSL growth rate would likely be higher but for the 25% price increase); ZDNet, *DSL Growth Slows, Lags Cable Modem Market*, available at <http://www.zdnet.com/products/stories/reviews/0,4161,2808053,00.html> ("The growth in DSL slowed as the economy weakened and service prices jumped by 15 percent to 20 percent to $50 a month ").

[229] *Third Section 706 Report* ¶ 70; *see also*, James K. Glassman, *Tauzin-Dingell: Network to Nowhere* (Feb. 7, 2002) ("Subscribers to digital subscriber line (or DSL) technology . . . increased 87% [last year]."

has deployed DSL to central offices serving 79% of access lines.[230] Similarly, Qwest announced a 77% increase in DSL customers, and SBC informed investors of a 69% increase.[231] SBC also reported that it has expanded its DSL-capable footprint by 37% to 25 million customers.[232] BellSouth announced that – due to "the most aggressive DSL deployment strategy in the industry" – the company enjoyed *188%* growth last year.[233] BellSouth's DSL deployment currently reaches 70% of households (15.5 million lines), up from 45% at the end of 2000, and the company anticipates passing 76% of households by the end of the year.[234] "We've had the best quarter we've ever had," reported the president of BellSouth Broadband and Internet Services, who also boasted that the company expects the number of broadband customers to nearly double in the coming year.[235] "We're pretty excited by the numbers," according to a BellSouth spokesman.[236] "Our goal was 600,000 subscribers by the end of the year, and we went substantially past that."[237]

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[230] News Release, Verizon, *Verizon Communication Reports Solid Results for Fourth Quarter, Provides Outlook for 2002* (Jan. 31, 2002).

[231] *See* News Release, Qwest, *Qwest Communications Reports Fourth Quarter, Year End 2001 Results, Jan. 29, 2002*; News Release, SBC, SBC Reports Fourth-Quarter Earnings (Jan. 24, 2002).

[232] *See id*.

[233] News Release, BellSouth, *BellSouth Captures 620,500 DSL Customers and Deploys Broadband Capabilities to More Than 15.5 Million Lines* (Jan. 3, 2002).

[234] *See id*.

[235] *Huge DSL Growth Likely*, *The Miami Herald* (Jan. 4, 2002).

[236] *BellSouth Logs Rapid Growth in DSL Connections*, *Money* (Jan. 4, 2002).

[237] *Id*. Similarly, in a letter published in *USA Today*, Verizon proclaimed that it is not "losing the high-speed Internet race" to cable companies. Letters, *Column Delivers Fuzzy Picture About Cable, USA Today* (Feb. 14, 2002). That race, Verizon insists, is "heating up, and the lead is

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The future also bodes well for DSL. RHK predicts that "the total number of North American DSL subscribers will grow from 4.75 million in 2001 to 15.76 million at the end of 2005."[238] This growth rate, 35%, exceeds the expected growth rate for cable modem service, 26%.[239] Other analysts – including Morgan Stanley, Gartner, Forrester, Yankee Group, Jupiter, and Forward Concepts – similarly anticipate stronger growth from DSL compared to cable.[240] Indeed, Cahners predicts that, by late 2004, cable modem access will no longer be the broadband access technology with the most subscribers in the United States.

Even the studies that SBC cites in its petition show DSL providers enjoying significantly higher growth rates than cable providers through 2005.[241] As SBC reports, Forrester predicts a 500% increase for DSL and only a 190% increase for cable from 2001 to 2005; Yankee Group predicts a 220% increase for DSL and only a 120% increase for cable from 2001 to 2005; Gartner Dataquest predicts a 230% increase for DSL and a 130% increase for

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narrowing each day," and "Verizon has assembled the assets, the scale and scope, and the technology base required to go head to head with cable," so that, in the end, "[Verizon] plan[s] to be a gold-medal winner in the high-speed Internet race." *Id*.

[238] RHK Telecommunications Industry Analysis, *Broadband Access: North America, Market Forecast: DSL 2001-2005*, at 5 (2001).

[239] *Id*. at 15.

[240] *See* Cahners In-Stat Group, *U.S. Residential DSL Continues to grow Despite Market Turmoil*, at 1 (Oct. 1, 2001) (expecting a nearly four-fold increase in U.S. residential DSL subscribers from 2001 to 2005); Cahners In-Stat Group, *Despite Service Provider Pratfalls, Cable Modem Subscriber Growth Remains Robust*, at 1 (Dec. 1, 2001) (expecting only about a two-fold increase in North American cable modem subscribers over same period); Morgan Stanley, *Residential Broadband Update*, at 37 (Dec. 28 2001) (projecting 3.7x increase in U.S. DSL subscribers from 2001 to 2004 and only 2.8x increase in U.S. cable subscribers over same period).

[241] *See* SBC Petition at 40.

cable from 2001 to 2004; Jupiter predicts a 360% increase for DSL and a 150% increase for cable from 2001 to 2005; and Forward Concepts predicts a 210% increase for DSL and a 150% increase for cable from 2001 to 2004.[242] SBC's assertion that "the cable operators in SBC's region have recently increased their market share" is contradicted by SBC's own evidence.[243]

To be sure, these studies show cable maintaining an overall advantage through 2005. But that is entirely to be expected, considering that ILECs voluntarily chose not to enter the advanced-services market for so many years, and thereby allowed cable providers to enter the market first.[244] Moreover, the ongoing success of cable modem service is not due to any "regulatory shackles" imposed on ILECs,[245] but rather to the facts that "[cable] service is cheaper and the installation lead-times are shorter compared with DSL."[246]

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[242] *See id.*

[243] *Id*. at 49.

[244] *See* Gartner, Inc., *U.S. Consumer Telecommunications and Online Market*, 2001, at 30 (Nov. 8. 2001) ("Gartner Dataquest believes that cable companies have the edge because of their first-to-market advantage.").

[245] SBC Petition at 6; *see also id*. at 52-53.

[246] RHK Telecommunications Industry Analysis, *Broadband Access: North America, Market Forecast: DSL 2001-2005*, at 10 (2001) ("In addition, cable providers have more aggressive marketing and bundle cable services more effectively with high-speed data services."). *See also* Cahners In-Stat Group, *U.S. Residential DSL Continues to Grow Despite Turmoil*, at 1 (Oct 2001) ("Cable is often a cheaper alternative to connect to the Internet in terms of monthly charges, a factor that holds more influence over consumers, especially since the U.S. economy is experiencing tough times."); Morgan Stanley, *Residential Broadband Update* 33 (Dec. 28 2001) ("The RBOCs seem to be more focused on entering long-distance, where minimal capital expenditures are required to address a $80 billion annual market. The RBOCs' historical focus on the business market has also hurt their residential broadband deployment."); Gartner, Inc., *U.S. Consumer Telecommunications and Online Market, 2001*, at 30 (Nov. 8. 2001) ("Gartner Dataquest believes that cable companies have the edge because of their first-to-market advantage. Cable companies have enjoyed this advantage as a result of their own aggressiveness and the myriad of problems encountered with DSL deployment. In various locations the price advantages of a cable model over DSL also acts against DSL taking the broadband lead."); (continued …)

Ironically, the only things standing in the way of continued rapid deployment are the ILECs and their relentless deregulation campaign. Contrary to SBC's unsubstantiated assertion that less regulation will lead to more investment, "history and economic theory have taught us" that the opposite is true with monopolists such as the ILECs.[247] "[A]s is well documented in the literature of economics, monopolists do not invest the full amounts required for economic efficiency when they are provided with monopoly returns on their investments."[248] A monopolist "will resist investing in new technology if its introduction will undercut the value of its existing assets."[249] And that is exactly what the ILECs did for years.[250] Fearing

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Broadband Intelligence, Inc., *Quarterly Report Analysis – Q3 2001*, at 1 ("The emerging pricing scheme positions cable modem prices at least several dollars below ILEC DSL rates."); Bill Scanlon, *SBC Blames Regs for Hard Times*, eWeek (Oct. 29, 2001) ("[I]nvestors scoffed last week, when SBC Communications Chairman Edward Whitacre blamed his company's third-quarter losses on government regulations that blocked SBC from deploying DSL."); Robert E. Hall and William H. Lehr, *Promoting Broadband Investment and Avoiding Monopoly* 8 (Jan. 21, 2002) ("Recnet disappointments in DSL are the result of the collapse of many of the new rivals, the subsequently higher prices charged by Bells once they no longer face competition, and because of the poor quality of service offered by the Bells which may have turned many would-be consumers away."); Willig Decl. ¶ 108 ("The high price that SBC charges for DSL also helps explain why its share is lagging so far behind that of its cable modem competitors.").

[247] Letter from William J. Baumol, Professor of Economics, New York University et al. to the Honorable Donald L. Evans, Secretary, U.S. Department of Commerce, at 3 (Dec. 12, 2001) ("Baumol Letter"); *see also* Willig Decl. ¶ 149 ("The best way to advance the twin policies of strengthening broadband competition and increasing broadband growth is to promote the CLEC sector."); Robert E. Hall and William H. Lehr, *Promoting Broadband Investment and Avoiding Monopoly*, at 2 (Jan. 21, 2002) ("Granting the Bells reduced regulation for broadband services would be a major shift in regulatory policy that would accomplish exactly the opposite of its intended effect: it would increase overall regulation, *it would decrease investment*, and it would reduce prospects for competition. In all these respects, it would harm consumers.") (emphasis added).

[248] Baumol Letter at 2.

[249] *Id.*

[250] *Id.*

cannibalization of their existing second line, ISDN and T1 services, the ILECs allowed dust to settle on potential DSL technology. And as carrier after carrier has stumbled or fallen, the RBOCs have responded with slower DSL deployments and higher prices.[251]

In addition, not only would deregulating ILECs' broadband services diminish ILEC investment in broadband, but it would also reduce competitors' investments in broadband.[252] "Because of the natural monopoly character of most local loops, unless these facilities can be leased by competitors on the same economic terms as the Bells provide them for their own use," competitors will have lessened incentives to invest in the electronic and other systems that would permit them to offer broadband services to customers.[253] Needless to say, "[t]he most important thing that the Administration can do to reinvigorate investment in advanced telecommunications networks and services is to improve Bell compliance with the 1996 Act."[254]

B. SBC's Regulatory Parity Arguments Are Baseless.

Lacking any facts to support its claim that the regulations at issue have had a

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[251] Willig Decl. ¶¶ 99-100.

[252] Baumol Letter at 3.

[253] *Id*.; *see also* Communication from the Commission to the Council, the European Parliament, the Economic and Social Committee and the Committee of the Regions: Seventh Annual Report on the Implementation of Telecommunications Regulatory Package, COM(2001)310 final at 18-22 (finding that one of the keys to competitive broadband access is opening up the local access network and recommending that the process be "speeded" up through "hands-on monitoring," "the setting of binding deadlines and the imposition of credible financial penalties on incumbents not complying with the requirements imposed").

[254] Baumol Letter at 4; *see also* Comments of AT&T, *Request for Comments Deployment of Broadband Networks and Advanced Telecommunications*, Docket No. 011109273-1273-01 (National Telecommunications and Information Administration, Department of Commerce) (Dec. 19, 2001); Willig Decl. ¶ 149 ("The best way to advance the twin policies of strengthening broadband competition and increasing broadband growth is to promote the CLEC sector.").

material impact on ILEC deployment of broadband services, SBC argues instead that cable companies are "completely deregulated,"[255] and that "fairness" therefore requires deregulation of ILEC broadband services. SBC's demand for "regulatory []parity"[256] is contrary to the relevant facts, economic reality, and the Telecommunications Act.

SBC's suggestion that cable companies are "completely unregulated" is fanciful. The truth is that cable companies are "differently regulated,"[257] that is, they are subject to a host of significant and burdensome regulations that do not apply to ILECs at all. Cable companies, for instance, must comply with local franchising requirements and pay billions of dollars in annual franchise fees.[258] They must build "institutional networks" for franchising authorities, and are subject to a host of "must-carry," PEG and other costly regulations.[259] ILECs face nothing similar. Cable companies also must confront the possibility of regulatory limits on the number of subscribers that they can serve.[260] ILECs do not. And finally, cable companies must provide access to their services without regard to the level of the residents' income.[261] ILECs, by contrast, can (and do) selectively deploy broadband services and avoid whole communities that

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[255] SBC Pet. 4.

[256] *Id*. at 5.

[257] Roll Call, July 23, 2001 (statement of Rep. John Conyers and Chris Cannon).

[258] *See id*.; *see also* Comments of AT&T, *Request for Comments Deployment of Broadband Networks and Advanced Telecommunications*, Docket No. 011109273-1273-01 (National Telecommunications and Information Administration, Department of Commerce) (Dec. 19, 2001).

[259] *See* 47 U.S.C. §§ 531, 532, 534, 535, 536.

[260] *Id.* § 533(f)(1).

[261] 47 U.S.C. § 541(a)(3); *see also Roll Call*, July 23, 2001 (statement of Rep. John Conyers and Chris Cannon).

could greatly benefit from high-speed Internet access. SBC makes no mention of these expensive, cable-specific regulations, offers no basis to compare the regulatory costs imposed on cable companies and ILECs, and makes no reasoned argument that regulations on the whole render ILECs worse off than cable companies.

Moreover, in requesting "equal" treatment, SBC disregards an overriding economic distinction between ILECs and cable companies that necessitates market-opening regulations of ILECs but not cable companies: ILEC networks, especially the local loop, remain "a quintessential bottleneck facility for competing telecommunications carriers" that ILECs can leverage to "perpetuate their monopolistic dominance of existing and emerging telecommunications markets."[262] Because of these entrenched, resilient local exchange monopolies, continued regulatory oversight is necessary to ensure that competitors can access ILECs' bottleneck facilities free of price-squeeze and unfair discrimination. By contrast, cable companies face substantial competition in their core video services and have no control over bottleneck facilities. Every cable company faces two facilities-based competitors, with all-digital platforms and a nationwide reach. Since 1993, the share of the multichannel video programming marketplace held by cable's competitors has increased to 20%, and four out of five new subscribers to video services now choose satellite over cable.[263] Because cable operators do not control bottleneck facilities, there is no corresponding regulatory concern that cable operators can exclude or marginalize other video programming by the manner in which they roll out high-

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[262] *See* Br. for Resps. at 22, *WorldCom, Inc.* v. *FCC* (D.C. Cir. filed Nov. 2, 2000) (No. 00-1002).

[263] *See Applications for Consent to Transfer of Control of Licenses, Comcast Corporation and AT&T Corp., Transferors, to AT&T Comcast Corporation, Transferee*, Application and Public Interest Statement, at 66-67.

speed Internet access services. In short, as a matter of economics, cable companies are not similarly situated with ILECs.

Finally, it is precisely because of this economic distinction that Congress, through the Telecommunications Act, mandated different regulations for cable companies and ILECs. Under the statute, for example, ILECs – and only ILECs – must unbundle their networks and offer interconnection at any technically feasible point.[264] Congress unmistakably decided not to impose similar requirements on cable companies. Indeed, Congress considered and expressly rejected a "regulatory parity" proposal prior to the enactment of the 1996 Act.[265]

As a result, what SBC is asking the Commission to do is to ignore the Act and enact a proposal that Congress defeated. Every item on SBC's "regulatory disparity" complaint list is a statutory requirement imposed by Congress. Thus, even if SBC were correct that cable companies are "completely deregulated," – and it is not – and even if ILECs and cable companies were similarly situated economically – and they are not – SBC's request to dismantle the current regulatory regime "in holistic fashion" would necessarily fail.[266]

If and when the ILECs' monopolies are broken and competitive local telephone markets emerge, it may well be appropriate for Congress and the Commission to reconsider the

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[264] 47 U.S.C. § 251(c).

[265] *See, e.g., Stevens Draft Includes 'Title VII' Provision; Senator Hopes to Include Language in Other Bills*, *Telecommunications Reports*, at 1-2 (Apr. 18, 1994); *White House Working to Include 'Title VII' in Telecom Bills; Hollings Says Provision 'Isn't Realistic At This Time*, *Telecommunications Reports*, at 4-6 (February 28, 1994). Under one version of this proposed framework, all providers of "advanced" services would have been subject to similar access and interconnection obligations. *See NARUC Adopts Package of Legislative Resolutions to Guide Negotiations on Fast-Moving Telecom Bills*, *Telecommunications Reports*, at 10-15 (Mar. 7, 1994) (describing specifics of proposed Title VII and NARUC's opposition thereto).

[266] SBC Petition at 7.

need to regulate access to the incumbents' networks. In today's marketplace, however, ILEC requests for "regulatory parity" are supported by no sound factual, policy or legal basis, and they instead carry the risk of devastating consequences for consumers and competition.

CONCLUSION

For the foregoing reasons, the Commission should deny the SBC Petition and clarify that any future ILEC petitions for exemptions from tariffing and other dominant carrier regulations will be denied absent clear and convincing proof – specific to the particular services, customer classes, and geographic areas for which the exemptions are sought – that the ILECs lack any relevant market power.

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March 1, 2002